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Corrections & Clarifications

In "Prepare for Change—Again" (Politics & Policy, Nov. 8-14), we incorrectly ran a photo of David Price (D-N.C.) instead of a photo of Hal Rogers (R-Ky.) of the House Appropriations Committee.

One Issue: Two Covers

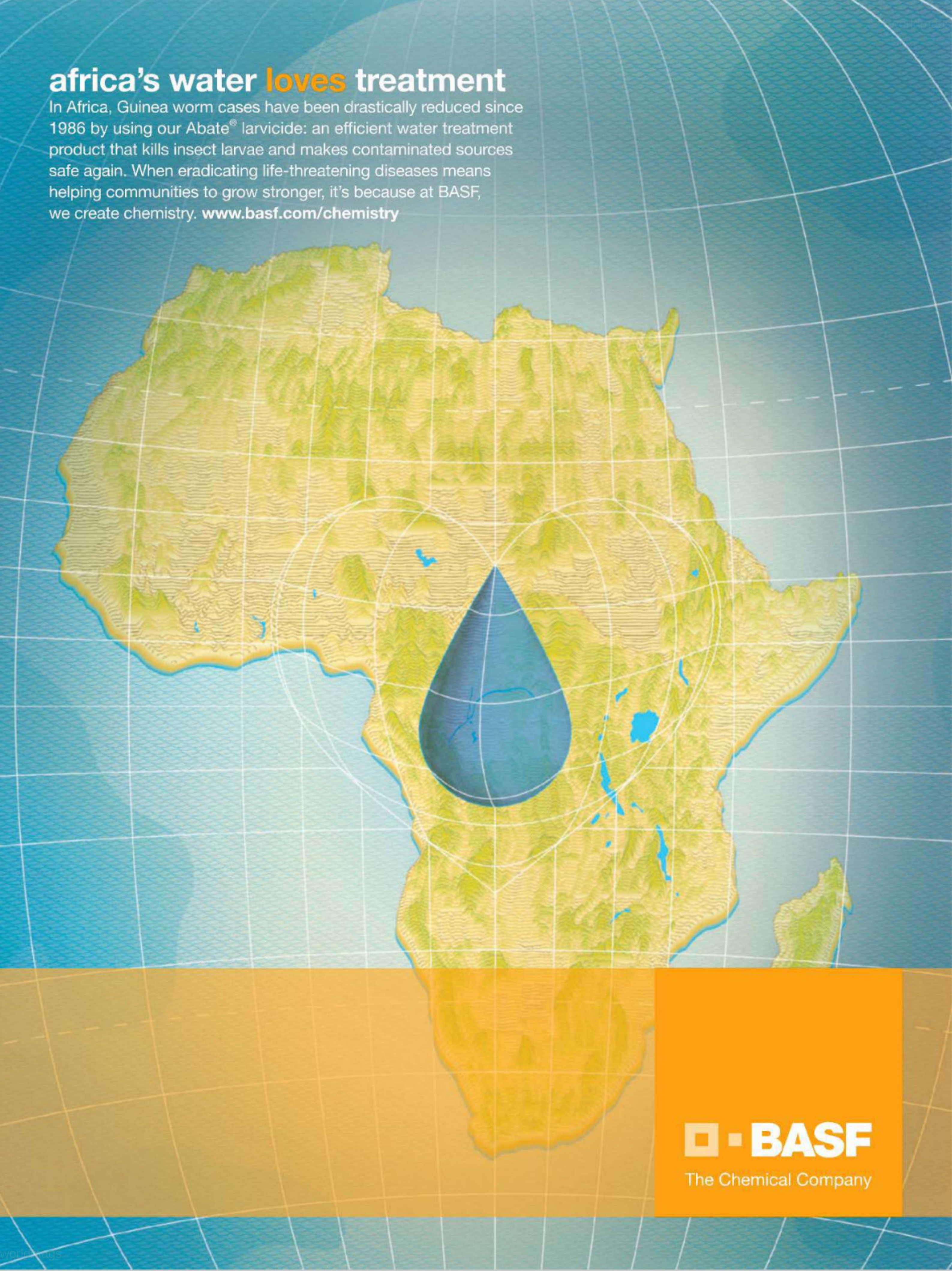
This week's *Bloomberg Businessweek* has a split cover. Subscribers received "Be Evil" by British illustrator HelloVon, while the newsstand edition features an illustration by Mexico City native Craig Robinson. Both issues have the same content. *Vive la différence!*



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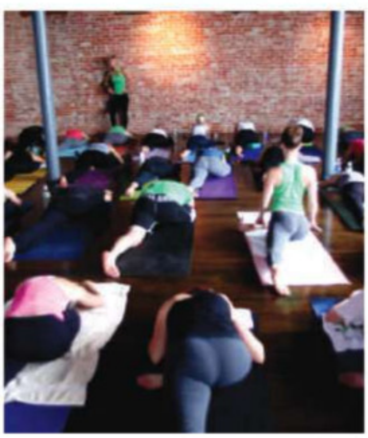
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Make Your Mark





A Winning Combo
YAS Fitness' alternate take on yoga and spinning has helped ex-attorney Kimberly Fowler (top) set her business apart from more traditional studios.

YAS Fitness Centers, with four locations in and around Los Angeles, was born out of frustration, as most revolutionary ideas are. Until ten years ago, however, YAS's founder, Kimberly Fowler, was content as a star attorney working her way up to partner.

YAS Fitness Centers Founder Kimberly Fowler's road to entrepreneurship began following a climbing accident years ago. To recover from her injuries, Fowler found that combining yoga and spinning was a potent combo. Yoga provided strength training and flexibility, while spinning, a cardio workout done on a stationary bike, boosted her endurance. However, no studio or gym offered both workouts under one roof, requiring Fowler to travel to multiple gyms to get both aspects of her exercise routine in back-to-back.

While this was a source of frustration at the time, within a few short years, Fowler recognized her frustration for the opportunity it was. The lack of a combined yoga and spinning class was a hole in the market—an opportunity for her to make her own mark on fellow fitness enthusiasts. So in 2001, she decided to open her own gym, offering both yoga and spinning, with YAS as the acronym for the unique workout combo.

> "The black sheep of yoga... My tagline is 'No chanting, no granola, no Sanskrit'"

Her vision was to create the "Cheers" of gyms, with Fowler herself as Sam the bartender. Her clientèle were people just like her – fitness fanatics in search of a better workout. And although she had originally pictured her gym on the outskirts of Los Angeles, she found the perfect space in Venice, Calif. – a dilapidated brick warehouse that formerly housed Bruce Lee's dojo 30 years ago. Over time, Fowler transformed it into a leading edge facility, helping to bring about change in the immediate neighborhood and in the fitness industry.

Convincing people that her yoga and spinning combo was superior did take some effort, however. There was some initial resistance to her non-traditional approach, both from instructors and from clients. Fortunately, it didn't take many workouts to convince them of its advantage. The results were impressive.

Even as she won over existing clients, attracting new clients remained a challenge, so Fowler did what many savvy business owners do—she studied what worked and what didn't at other yoga studios. Then she took what worked well and incorporated changes at YAS. One of her big changes initially was to cut her classes from 90 minutes to 60 after witnessing most clients walking out at the one-hour mark. Daring to shorten the sacred 90-minute yoga session made Fowler "the black sheep of yoga," she says.

However, that stigma didn't last long and soon other studios began trying to copy Fowler's innovative workout. None were successful, mainly because Fowler had already established herself as an unconventional business owner. She had made her mark among Type-A athletes who would normally feel uncomfortable in a traditional yoga environment; they flocked to YAS. Reflecting that rebel streak, Fowler says, "My tagline is 'No chanting, no granola, no Sanskrit.'"

Today, YAS Fitness Centers are planned for cities well beyond her current four locations in Los Angeles. Fowler has also debuted a popular line of sportswear under the YAS label. She continues to make her mark by separating herself from the pack. "That's what makes your mark—what makes you different."

To learn more about YAS Fitness, tune into Bloomberg The Mentor® to see where small business gets the lifetime experience of successful CEOs. Only on Bloomberg TV, Thursdays at 9pm.

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Opening Remarks

What's the Rush?

The American financial system is erratic and voracious, and keeps score in milliseconds. Here's how to rein in the beast
By Peter Coy



GREGOR SCHUSTER/GETTY IMAGES

Shares of Accenture, the big tech consulting firm, were selling for $40 on the afternoon of May 6 when the stock suddenly seized up. For 22 seconds there were no recorded trades. Then came a transaction below $10. In the next eight seconds, Accenture quivered like a fibrillating heart, its price changing more than 80 times before flat-lining at one penny. Then just as abruptly–"Clear!"–the share price rebounded to $40 and stayed there. The super-low trades have since been reversed by the exchanges but the record of them lives on in Bloomberg's database.

Accenture was just one of the many companies whose shares were wracked by the May 6 crash, known to many as the "flash crash," which briefly reduced the value of U.S. stocks by more than $800 billion. The vast liquidity that automated trading systems supposedly provide the stock market vanished instantly that day, as computer programs shut down in confusion. Now it's becoming clear that May 6 was not a one-time convulsion. *The New York Times* reported on Nov. 9 that more than a dozen individual stocks, including Progress Energy, Citigroup, and Washington Post Co., have suffered mini-crashes in the months since. As Andrew W. Lo, director of the Laboratory for Financial Engineering at Massachusetts Institute of Technology, told the *Times*, "The U.S. equity markets have become the Wild, Wild West."

There's a familiar–and odd, and unfortunate–echo here. Banks on Wall Street and Main Street overlent, leading to the worst economic downturn since the Great Depression. Then they got bailed out. Then they paid big bonuses. Now they are cranking up their trading operations in a way that imperils the financial system once again. Gary Gensler, a former Goldman Sachs executive who heads



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Opening Remarks

Heart Attack

On May 6, computerized trading went haywire. For two minutes, Accenture's stock was a victim.

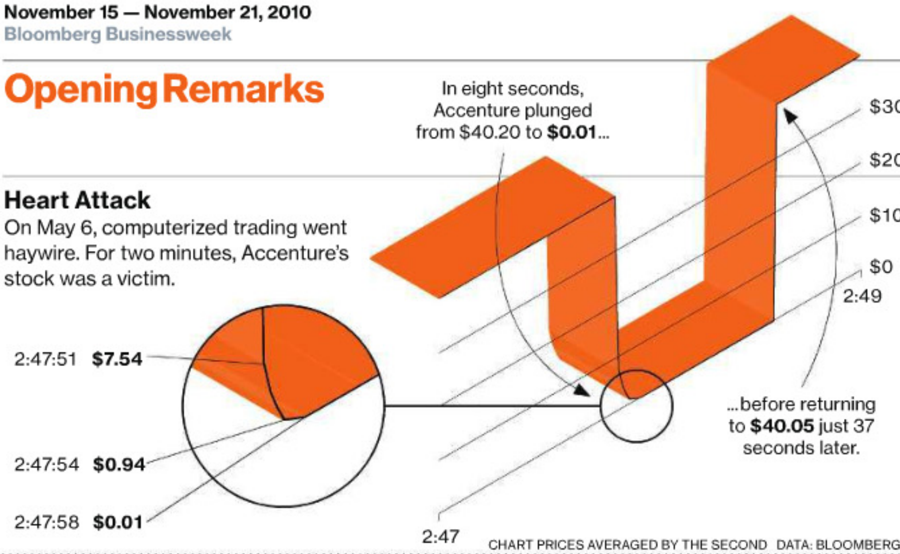


CHART PRICES AVERAGED BY THE SECOND DATA: BLOOMBERG

the Commodity Futures Trading Commission, last month compared one firm's trading strategy in the May 6 crash to driving on "autopilot into a ravine."

Fixing this is not a matter of patching up the current system, as the Securities and Exchange Commission is already doing (see page 58). It's time to step back and consider the proper role of finance in the American economy. Right now finance is an erratic master. It ought to be a quiet, efficient servant.

Harvard University economist Benjamin M. Friedman asks the right question—"Is our financial system serving us well?"—in an essay in the fall 2010 issue of *Daedalus,* the journal of the American Academy of Arts and Sciences. Friedman points out that from the 1950s through the 1980s, profits earned by financial firms excluding insurance and real estate accounted for 10 percent of total U.S. profits. Finance's share of profits grew to 22 percent in the 1990s and to an astonishing 34 percent from 2001 to 2005. Fantastically high salaries and bonuses attracted more than a quarter of Harvard's graduating job seekers to investment banks, hedge funds, private equity firms, and the like. That, Friedman notes, was "just before the surge in borrowing, securitization, and derivatives finance began to transform itself into a world-class crisis."

The bigger the financial sector gets, the more dangerous it becomes. The high-frequency trading that contributed to the May 6 crash is a case in point. High-frequency traders are engaged in a costly technological arms race to decrease the "latency" of their trades so they can exploit fleeting arbitrage opportunities before their rivals do. Peter Duffy, chief technical officer of Glasgow-based Sumerian, a trading analytics firm, says one of his firm's clients in the City of London has more computing power in one segment of its equity-trading operation than the entire British nation had in 1985. In high-frequency equity trading, says Duffy, the goal is to take in market data, process it, and get a buy or sell order back out all in less than 2 milliseconds.

These vast resources are being spent on a zero-sum game. Any incremental gain for the seller is a loss for the buyer, and vice versa. Backers of high-frequency trading say they add liquidity to the market, making it easier for ordinary investors to buy or sell without causing the market to move against them. But liquidity is worth nothing if it goes away when it's most needed, like a swimming pool that dries up just as you jump off the high dive. In the May 6 crash, spreads widened beyond belief. Trades were done at prices from as low as one penny a share to as high as $100,000 a share.

One proposed solution gathering support is a transactions tax—possibly just a few cents per $100—that would throw sand into the gears of high-frequency trading. The European Parliament came out in favor of the concept earlier this year. Britain already has a half-percent "stamp duty" on stock sales that traces its origins to 1694; it hasn't kept London from being one of the world's chief financial centers.

Last year in Pittsburgh the G-20 leaders asked the International Monetary Fund to look into the idea of taxing stock sales. In a detailed review released in September, IMF economist Thornton Matheson concluded that a global transactions tax would be feasible, though not the ideal solution either for raising money or for dampening debt-fueled speculation. "The buildup of hidden financial risks in the recent crisis," Matheson writes, "resulted predominantly from excess leverage, risk concentration and product innovation such as asset securitization, which would have been largely unaffected by a transactions tax."

Maybe the answer is something more drastic than a transactions tax. As Matheson writes in the IMF document, there are other options for attacking debt-fueled speculation. These include demanding higher margin and collateral. Or taxing debt on the balance sheet, which would encourage companies to sell shares to pay down debt. Or limiting the deductibility of corporate interest payments so companies are no longer encouraged to load up on debt. Market structures could be made safer, too. Adam Sussman, head of research for the TABB Group, a New York-based financial markets research and advisory firm, says the high-frequency arms race was inadvertently launched by the SEC itself in 2006 when it approved a regulation allowing exchanges to bypass other exchanges that didn't respond quickly, even if they had the best prices. Says Sussman: "The SEC was basically guaranteeing that we would see more strategies that depended on speed."

Any effort to make finance safer, especially via new taxes, will be vociferously opposed by Wall Street and the banks, whose profits are amplified by leverage. Of course, the financial industry has powerful allies in Washington. When the SEC toughened its trading rules after the crash last May, Eric Cantor, who's set to become House majority leader, scolded the agency. "I am concerned that this was done before conducting a holistic review of the causes of the disruption," Cantor, a Virginia Republican, wrote to the SEC on May 21. Bloomberg News reported on Nov. 9 that high-frequency trading firms with names like Getco, Hard Eight Futures, and Quantlab Financial have more than quadrupled their political giving over the last four years; Cantor was one of the high-frequency traders' top recipients, getting $23,000 since the start of 2009 for himself and his political action committee. (Cantor wasn't available to comment for the Bloomberg News story, his spokesman John Murray said.)

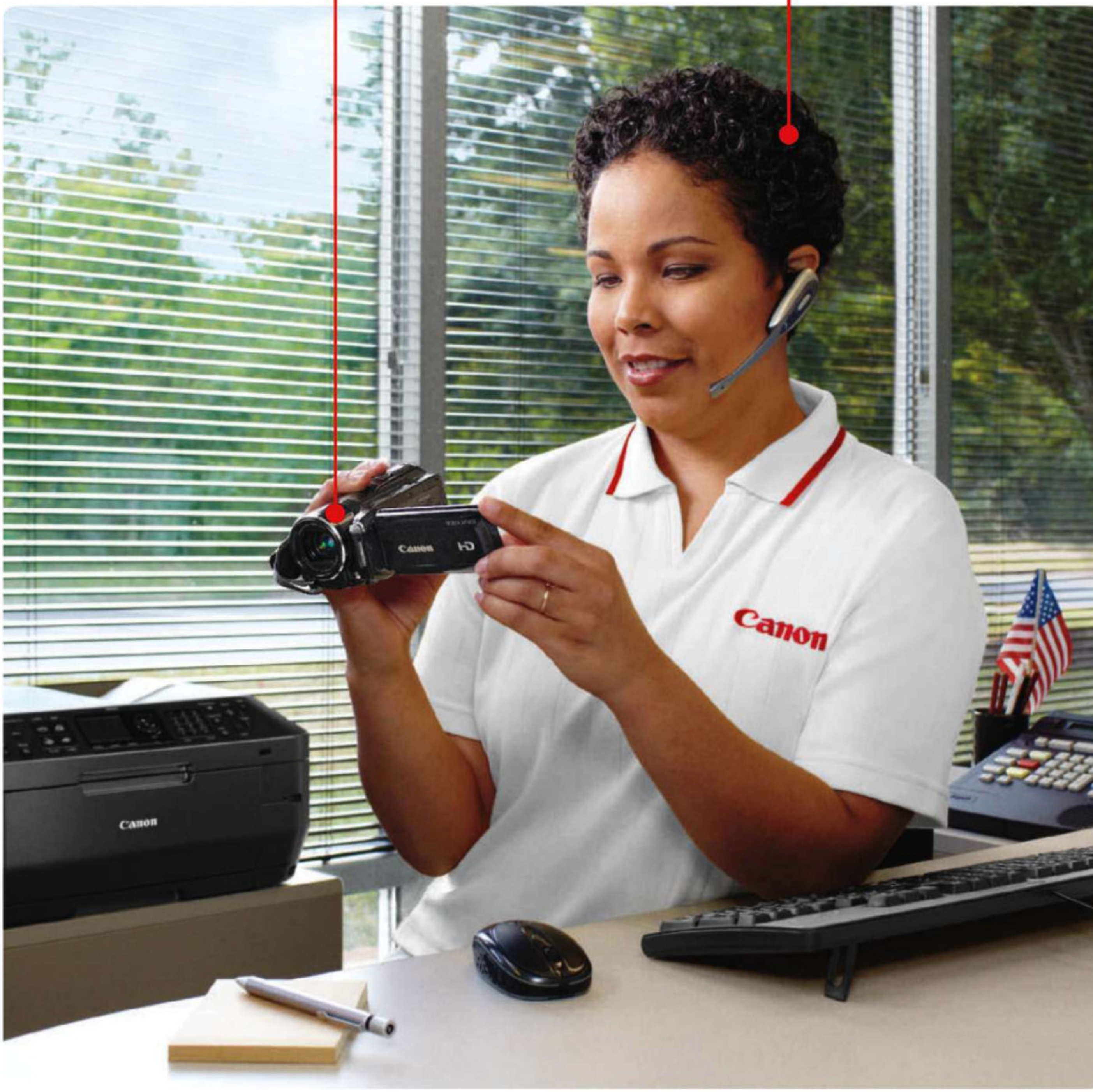
Most taxes are a necessary evil. Taxes on labor income discourage work. Taxes on dividends and capital gains discourage investment in new factories, office buildings, equipment, and software. What would new taxes on Wall Street discourage? High-frequency trading and overleverage. Hmm. They just might be the rare taxes that the public would support. B

—With Jesse Westbrook, Robert Schmidt, and Frank Bass

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Global Economics



Welcome, G-20: The financial confab in Seoul is expected to be tense

Asian Leaders at G-20 Brace for a Flood of Dollars

▶ On the eve of the Seoul meeting, the region's officials consider controls on capital

▶ "One of the worst jobs in the world next year is being an Asian central banker"

It's called the impossible trinity, and it's an economist's way of saying "you can't have your cake and eat it too." Conceived by Nobel Prize winner Robert A. Mundell and International Monetary Fund economist Marcus Fleming in the 1960s, the hypothesis states that no country can have an open capital account (in which portfolio and direct investment moves in and out of a country freely), a fixed or closely limited exchange rate, and an independent monetary policy. It's certainly possible to pursue two of the three policies successfully. If a country's government tries all three, however, something has to give.

The impossible trinity is a fascinating concept for academics: Now it's turning into a painful reality for the central bankers and finance ministers of Asia. As interest rates and growth have sagged in the U.S., investors have poured their money into the still immature markets of Asia, placing unbearable upward pressure on currencies, driving asset prices and stocks sky-high, and stoking the fires of inflation.

With officials headed to Seoul for the meeting of the Group of 20 economies, the representatives of China, Korea, Indonesia, and other countries were expected to voice their anxiety over the challenges they face. They have already vented freely at the Federal Reserve for its plan to spend another $600 billion on asset purchases to lower U.S. rates even further.

> "This 'impossible trinity' dilemma is starting to bite. They face capital inflows that can be destabilizing"

Until recently, many Asian governments allowed free flows of capital and kept their exchange rates fixed. To keep their currencies from rising, they often printed money and bought dollars with it. In effect, they adopted the easy-money policy of the Federal Reserve. Asian policymakers now are starting to realize that they can't have

KIM JAE-HWAN/AFP/GETTY IMAGES

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it all. "One of the worst jobs in the world next year is being an Asian central banker," said Robert Subbaraman, Nomura Holdings' chief economist for Asia excluding Japan. "This 'impossible trinity' dilemma is starting to bite. They are facing capital inflows that potentially can be very destabilizing."

Asia has attracted $2.3 billion of capital daily since April 2009, according to DBS Group Holdings. Stock markets in India, Indonesia, Malaysia, and the Philippines have reached record levels. The MSCI Emerging Market Asia Index of stocks has advanced more than 17 percent this year, compared with 9 percent for the Standard & Poor's 500-stock index. All of the region's major currencies, except the greenback-pegged Hong Kong dollar, have strengthened, even as policymakers across the region seek to stem the gains to keep exports flowing.

6

The number of times India's central bank has raised interest rates this year

In India, where the central bank has raised interest rates six times this year, officials acknowledge the dilemma: If they jack up rates to smother inflation, they also lure foreign money in search of double-digit returns. The outside money in turn inflates prices in real estate and stocks–which forces the central bank to push up rates even more. "At the national level, we have to manage the impossible trinity," **Reserve Bank of India** Governor Duvvuri Subbarao said on Oct. 27 in Mumbai. "Managing exchange rates in the face of volatile inflows entails a cost no matter what you do."

To avoid another flood of foreign capital, the central banks of Malaysia, Thailand, and Korea have paused in raising interest rates. The central banks of Indonesia and the Philippines haven't lifted rates. Yet central banks may fall "behind the curve" should they keep borrowing costs low, even as inflationary pressures increase, says Chetan Ahya, an economist at Morgan Stanley in Singapore. China held steady on rates until October. Now the government may miss its goal of keeping inflation to 3 percent this year, Zhang Ping, head of the National Development and Reform Commission, said in early November.

Capital controls may be the only answer for some governments. To make outside investors pause, Thailand last month removed a 15 percent tax exemption for foreigners on income from domestic bonds. On Oct. 29, Thai central bank Governor Prasarn Trairatvorakul said he wouldn't rule out controls if the baht's appreciation accelerates.

In South Korea, where a bank tax and a levy on financial transactions are under consideration, central bank Governor Kim Choong Soo has said capital controls may be "useful." The Indonesia central bank said it may extend a holding period for foreign purchases of central bank notes to three months from one. "We are going to see more capital controls," says Robert Prior-Wandesforde, head of India and Southeast Asia economics at Credit Suisse in Singapore. "QE2 [Bernanke's policy of bond purchases] will just accentuate it." Above all, Asia does not want its economy affected by decisions made in Washington, says Nomura's Subbaraman. "We need to set economic policy based on our own cycle."

—Shamim Adam

***The bottom line** Asian central banks realize they cannot have free capital flows, controlled currencies, and low rates at the same time.*

Real Estate

London's New Towers Could Augur Trouble

▶ The U.K. capital has a history of building big just before hard times

▶ Here come the "Cheese Grater" and the "Shard:" Is double dip next?

If hemlines tell which way the stock market is headed, maybe city skylines do the same for the economy. Tall stories often have unhappy endings.

That thesis certainly holds up in London, where new towers are sprouting. **British Land**, the U.K.'s second-largest real estate investment trust, has revived plans for a 47-story tower in the City of London dubbed the "Cheese Grater." **Land Securities Group**, its bigger rival, has found backers for its "Walkie-Talkie" building, which will be 10 floors shorter. Next to London Bridge, cranes are attaching glass panels to the soaring frame of the "Shard of Glass." Designed by architect Renzo Piano, the 1,017-foot (305-meter) pyramid will dwarf the other buildings north of the Thames to become Britain's tallest.

The history of this global capital suggests vertical ambitions often presage a southerly direction for the economy. In mid-2004,



Leadenhall Building
Construction on the skycraper, nicknamed the "Cheese Grater," was stopped. It will restart in January.

Shard London Bridge
When completed in 2012, this sliver of a high rise will tower over the City and become the tallest building in Europe.

20 Fenchurch St.
Near St. Paul's, this building, dubbed the "Walkie-Talkie," has triggered controversy because of its distinctive shape.

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Can Santa move the merch? page 30 ▶

Britain was enjoying its 48th consecutive quarter of gross-domestic-product growth, while **Swiss Reinsurance** was moving into a 40-story edifice in central London nicknamed the "Erotic Gherkin" for its resemblance to a swollen pickle. Four years after the Gherkin opened for business, the British economy was in recession, and continued to shrink for five quarters.

In 1990, Canary Wharf Tower stuck its head in the clouds to become the U.K.'s tallest structure at 800 feet. The economy grew 4.3 percent in July of that year. Once Canary Wharf was completed, the economy shrank in five of the next eight quarters. Before Canary Wharf, London's tallest building was the NatWest Tower, at 600 feet. The NatWest Tower's completion coincided with the 1980 slump.

That building is now named Tower 42. If you look west from the top floor's aptly named Vertigo bar, you can see the Post Office Tower, the previous record holder. At 580 feet, excluding a 40-foot antenna, the Post Office Tower started beaming radio and television signals in 1964. Three years later, the government had to devalue the pound.

Now some economists fear budget cuts will trigger a recession. Land Securities just opened the City's biggest mall, with 220,000 square feet of retail space fighting for customers—eight days after Chancellor of the Exchequer George Osborne detailed more than 80 billion pounds ($128 billion) of spending cuts and 490,000 public-sector job losses.

The edifice effect isn't restricted to London. The onset of the Great Depression coincided with the construction of New York's Chrysler and Empire State buildings. In Dubai, the $1.5 billion Burj Khalifa building is now the world's tallest. A month after the tower opened, Dubai needed a $10 billion lifeline to avoid default.

Why are tall buildings leading indicators of recession? Possibly because the backers conceived of their grand designs when the good times were so good that no one ever thought they would end. Developers might want to ponder these lessons before their ambitions get the better of their reduced circumstances. —*Mark Gilbert*

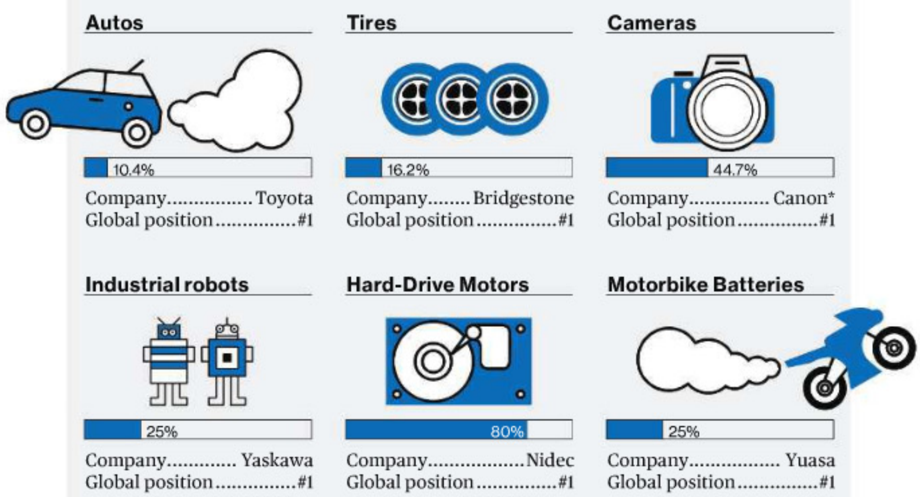
The bottom line *London is home to some grand construction projects. Unfortunately, tall towers often foreshadow shrinking economies.*

TOP: PHOTOSHOT HOLDINGS LTD./ALAMY

Competitiveness

Japan: Still in the Game

Japan has lost its position as the world's second-biggest economy to China, its government is struggling to contain the budget deficit, and growth is elusive at best. Japanese companies, though, are faring better than Japan, the country. Many remain dominant globally in industries big and small.



*SLR DIGITAL CAMERAS

DATA: COMPANY REPORTS; IDC

Currencies

German Might Trumps Irish Jitters

▶ Exports to Asia may trump credit worries about Ireland and Greece

▶ "If Germany does well, others do well too"

Credit markets have been thrown into a tizzy in recent weeks as investors focused on Ireland and Greece, two euro zone countries with world-class fiscal problems. Now markets are wondering how this will affect the euro, a currency that has been on a tear thanks to Germany's export-fueled growth.

Markets certainly fear an Irish flame-out. Irish bond yields have climbed to records relative to German bunds, reflecting heightened default risk. An index of credit-default swaps, which measures the cost of protecting investors in Greek, Irish, Portuguese, and Spanish government bonds from nonpayment, has more than doubled since May 12.

Yet the euro has climbed 9 percent since May, and at a recent value of $1.37, it is a healthy distance away from a four-year low of $1.19 on June 7. Goldman Sachs analysts even predict the euro will strengthen to $1.55 in a year.

The euro's relatively strong performance signals confidence that the euro zone countries collectively have the firepower to handle another sovereign debt crisis. The zone's officials pledged in May to back any struggling members by tapping the European Financial Stability Facility, which will make up to $1 trillion in loans and guarantees available if things get dire. "Earlier this year, the currency market was worried that the euro zone would not survive politically," says Thomas Stolper, an economist at

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Auctioning ad slots: State giant CCTV uses network stars to sell time

Goldman Sachs in London. "But now if there is a fire in one of your rooms, it no longer means that the whole house will go up in flames."

This cautious optimism stems from traders' new sense of proportion as they assess risk in the euro zone. "It's only when the big countries like Spain get involved that it's relevant for euro-dollar," says Bilal Hafeez, global head of foreign-exchange strategy at Deutsche Bank in London. Greece, Ireland, and Portugal are less consequential because "in GDP terms they're tiny, they're like Idaho. Right now it's the Germanic aspects of the euro area that are driving" the currency, he says. Ireland's gross domestic product accounted for just 1.8 percent of the euro region's $12.6 trillion economy last year. German output, in contrast, amounted to 27 percent.

Germany's exports have rebounded from a four-year low in May 2009, largely fueled by Asian demand. German gross domestic product has grown for five consecutive quarters since the nation emerged from recession in the second quarter of 2009, including a 2.2 percent jump in the three months through June. Traditional export titans like chemicals maker **BASF** and **Bayerischen Motoren Werke** have recorded strong profits.

The Germans are not even fazed by the recent strength of the euro, arguably a drag on their exports. For Raimund Muecke, a German pensioner from the Frankfurt suburb of Harheim, the euro's surge since June against the dollar signals a return to the days when a thriving Germany and an appreciating deutsche mark powered a robust Europe. "A strong euro is good for Germany," says Muecke, 63, who, along with his wife, was babysitting his grandson at a farmer's market one day in early November. "If Germany is doing well, others do well too."

Signs are emerging that the euro may be peaking, despite the bullishness of some analysts. The currency is off its recent high of $1.42 and jitters about Ireland and Greece won't go away. Traders are also gradually shifting their focus to the region's fiscal challenges. Europe may well prevail if another sovereign debt crisis erupts. A second big bailout won't be a pretty picture, though.

—Matthew Brown and Paul Dobson

The bottom line *Robust German export growth is powering the euro, despite market jitters about the debt crises in Ireland and Greece.*

Quoted

"The serious defects in the U.S. economic development and management model will lead to the long-term recession of its national economy, fundamentally lowering the national solvency."

—Nov. 9 report lowering the credit rating of U.S. sovereign paper from Beijing's Dagong Global Credit Rating. Pictured at right is Dagong Chairman Guan Jianzhong



Consumers

China's Marketers Scramble for Airtime

- Need to reach Chinese shoppers? You need *Country Love*
- "Grasp the opportunity. Take it in your hands. Believe in the brand"

Eight is a lucky number in China and, in Chinese, rhymes with "wealth." So at 8:08 a.m. on Nov. 8 state broadcaster **China Central Television** (CCTV) opened the annual bidding for its hottest advertising slots. Representatives of more than 280 Chinese and foreign companies bid for airtime on everything from *Country Love*, a popular drama set in rural northeastern China that is slated to run in next year's prime time slot on CCTV 1, to that precious minute following the 7:30 p.m. weather report. "Grasp the opportunity. Take it in your hands," intoned the nattily dressed auctioneer. "Believe in the power of the brand." CCTV even summoned the stars from its top programs to jazz up the auction.

By the time the gavel fell on the final bid at 8 p.m., $1.9 billion had been committed for next year's slots on CCTV's dozen-plus channels, 16 percent more than last year and a record high for the 17 years the auction has been held. Although well-known multinationals **Volkswagen** and **Procter & Gamble** were big

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spenders, local companies dominated. Milk and ice cream marketer **Mengniu Dairy** bid the highest, $34 million, to sponsor the fourth season of *Country Love*, which as many as 100 million Chinese will watch. "Any company that wants to be seen as a leading brand must get [its] products shown on CCTV," says He Dang, chairman of Nasdaq-listed **Charm Communications**, a media agency that represented more than 20 companies in the auction.

173%

Gain in urban per capita income in China since 2000

The golden age of television advertising, a distant memory in the U.S., is coming into its own in China. Urban per capita income is up 173 percent since 2000, to $2,515. WPP Group's investment arm, GroupM, expects mainland sales for liquor, household appliances, autos, and office products to reach $45 billion this year and $50 billion next year. While China's ad industry is growing at a double-digit rate, globally the ad market is expected to expand just 3.6 percent this year.

What makes advertising in China special is the continued dominance of the airwaves. GroupM figures 63 percent of total ad spending goes to TV, vs. 44 percent in the U.S. CCTV gets a third of that money, with the rest going to 1,000 provincial and local stations, including some powerful regional broadcasters in Hunan and Shanghai.

Digital marketing, up almost one-third this year in China, still accounts for only 8.8 percent of ad spending. "CCTV is viewed as the authoritative voice of the state. It is credible, reliable, and influential," says Jin Yibo, assistant to the president at Wuhu (Anhui)-based **Chery Automobile**, which spent $7 million for a slot during *Country Love*.

TV still leads in part because it's hard to measure the Internet's reach in China. Low broadband penetration in rural areas also limits the impact of digital media. Perhaps most important is the tube's track record. "In recent years we have achieved over 50 percent growth in sales annually," says Xu Xinjian, president of Jiangsu-based **Sunrain**, an alternative energy company that first promoted its solar water heaters on CCTV in 2002. "That has shown it is the right platform and medium for us to advertise on."

Other marketers have the same experience, says Andrew Carter, the Shanghai-based director of tactical planning at GroupM China. "If you are a company and are advertising on TV and getting double-digit growth, why change things?"

—*Dexter Roberts*

The bottom line *China's embrace of brands is driving a big increase in ad spending. Television, especially state TV, is a big beneficiary.*

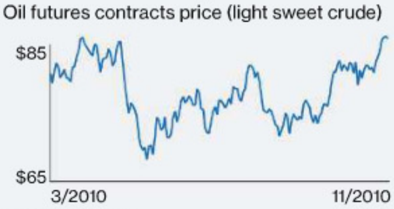
Energy

$100-a-Barrel Oil? Place Your Bets

▶ **The weakening dollar could trigger a steady rise in the price of crude**

▶ **Oil's Recent Runup**

Oil futures contracts price (light sweet crude)



DATA: BLOOMBERG

Oil prices have hovered around $78 a barrel most of the year, providing little excitement as other commodities, including copper, gold, and cotton, have enjoyed record runups. Global economic growth has not been brisk enough to drive up oil demand substantially, U.S. inventories have been ample, and the Saudis have been pumping enough to guarantee a plentiful supply.

A change in the oil markets may now be upon us. Crude may climb past $100 next year as central banks pump cash into their economies to revive growth, predict JPMorgan Chase and Bank of America Merrill Lynch. The Federal Reserve's decision to buy $600 billion of Treasuries from commercial banks should lower U.S. interest rates and weaken the dollar further. Investors may turn increasingly to oil and other commodities to get a decent return.

The Federal Reserve's actions

➜



LIOR MIZRAHI/AFP/GETTY IMAGES

Speed Dial Benjamin Netanyahu

Israel's Prime Minister on growth, security, and infrastructure

Israel's economy has performed impressively–4 percent growth ... .
Five percent, actually.

O.K. So what does Israel do to protect itself from economic turmoil elsewhere?
There is a tremendous opportunity to generate internal reform independent of what's happening in the global marketplace. Our 5 percent growth, for example, did not take place in real estate and construction. It's virtually impossible to build anything in Israel. Just by making the availability of land and the planning of construction easier, we can get an additional 1 to 2 percent growth a year for the next 10 years, independent of the U.S. and China.

You also have ambitious rail and road plans.
We've just decided on investing 27 billion shekels on fast roads and on expanding our rail system. We're cutting through a lot of red tape to do it. Slashing bureaucracy is one of the few pleasures I derive from public life.

There are estimates that a successful peace effort with the Palestinians could add to growth.
There is potential. Some of our peace partners have not fully appreciated the possibilities of economic growth for them. Economic peace benefits all parties. In the West Bank we've removed over 400 roadblocks to facilitate the movement of goods and people in the Palestinian Authority economy. That's been one of the factors behind their impressive growth. It's over 8 percent. That's made a world of difference.

—*Jonathan Ferziger, Kenneth Fineman, and Christopher Power*

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Global Economics

are "likely to push prices upwards," says Antoine M. Halff, head of energy research at Newedge USA in New York and former principal administrator at the International Energy Agency. "The past few years have shown that the more cheap money in the system, the more money flows into commodities, in particular energy." Since the start of September, oil prices have climbed 17 percent, to a recent $86.96.

Oil analysts are also watching OPEC for signs of its intent. Cartel members may seek a higher price as the depreciation of the greenback erodes the profitability of their dollar-denominated exports. Saudi Arabia's Oil Minister, Ali Al-Naimi, said in Singapore on Nov. 1 that a range of $70 to $90 a barrel should be satisfactory for consumers. The kingdom had previously indicated a target of $75 a barrel. "Al-Naimi spoke of a $70-to-$90 range for the first time," says Francisco Blanch, head of global commodity research at Bank of America Merrill Lynch Global Research in New York. "The next threshold is $90 if Al-Naimi says he won't be putting any more oil in the market until we get to that level." Later, however, OPEC's secretary-general said the group was satisfied with a range of $70 to $85.

Growth in emerging markets will help reduce stockpiles of crude oil in 2011, says David Greely, head of energy research at Goldman Sachs in New York. The Paris-based IEA figures global oil demand will climb from 86.9 million barrels a day this year to 88.2 million in 2011. Hedge funds and other large speculators are getting into the act: They increased their wagers on rising crude prices in late October, according to the Commodity Futures Trading Commission.

There are still skeptics about $100-a-barrel oil, such as Sarah A. Emerson, managing director of Energy Security Analysis in Wakefield, Mass. There's plenty of crude to satisfy world demand without spurring a dramatic climb in prices, says the energy analyst. "This is a well-supplied market, and that won't be changing anytime soon," Emerson says. "At the end of the day, fundamentals matter." Ⓑ

—Mark Shenk and Grant Smith

The bottom line *After several years in the doldrums, oil prices are creeping upward. Some analysts are projecting prices at $100 a barrel by next year.*

Seven Days

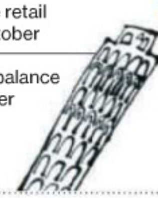
Events of note in the week ahead

by Ira Boudway

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U.S. advance retail sales for October

Italy's trade balance for September



▶ **China's Leading Economic Index:** The Conference Board launched its Chinese index in May. It has increased an average of nearly .6 percent every month since.



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Spain's Leading Economic Index

Earnings reports from Saks, Abercrombie & Fitch, Home Depot, and Target

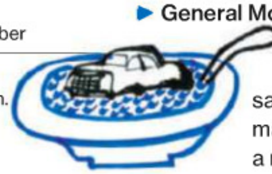
▶ **Wal-Mart Stores earnings report:** The retailer plans to boost headcount 36 percent in the next five years.

▶ **Obama's children's book:** *Of Thee I Sing: A Letter to My Daughters* hits bookstores.

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U.K. jobless claims for October

Republican Governors Assn. conference in San Diego



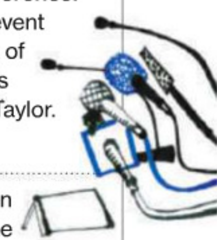
▶ **General Motors IPO:** The bailed-out auto giant plans to raise $10.6 billion with the sale of 365 million shares, making the U.S. government a minority shareholder.

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Bank of Japan minutes from Oct. 28 board meeting

U.S. Leading Economic Index

▶ **Cato Institute Monetary Conference:** Speakers at the 28th annual event include Federal Reserve Bank of Philadelphia President Charles Plosser and economist John Taylor.



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Harry Potter and the Deathly Hallows Part 1 premieres

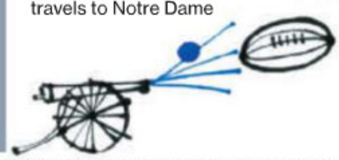
Earnings reports from Ann Taylor and Williams-Sonoma



▶ **Bernanke in Frankfurt:** Sixteen days after announcing the Federal Reserve's monetary easing plan, the Fed chairman speaks at a European Central Bank conference.

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College football: Army travels to Notre Dame



▶ **North London Derby:** Arsenal and Tottenham Hotspur renew their 123-year-old rivalry at Emirates Stadium.

21

Men's tennis: Barclays ATP World Tour Finals



▶ **German Finance Ministry monthly report:** Finance Minister Wolfgang Schäuble has been sharply critical of the U.S.'s recent monetary easing



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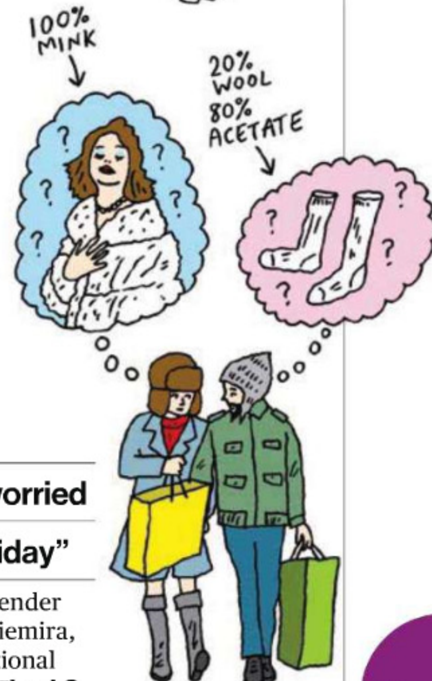
Contents ▶ The power of pop-up stores 26 ▶ Yes, Virginia, there is a digital Santa 27 ▶ Britain's holiday feast 28 ▶ Luxury consultant Robert Burke on what still sells 28 ▶ Retailers' big bets 29 ▶ No holiday cheer for China's toymakers 31 ▶ Company briefs 32 ● Edited by James E. Ellis











Will They Shop?

▶ Upscale stores see brisk sales, but mass marketers are worried

▶ "The luxury consumer will be the stellar spender this holiday"

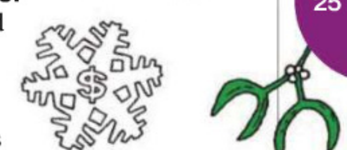




Just in time for the holidays, industry analysts are engaging in their annual ritual of trying to predict how much people will spend and what they buy this season. Amid the uncertainty about the U.S. economy, predictions have been as scattered as ornaments on a tree. AlixPartners, based in Southfield, Mich., says sales will be flat compared with last year. Customer Growth Partners of New Canaan, Conn., projects a 4.5 percent gain.

On this, at least, there's consensus: Luxury retailers are likely to hear silver bells at the register this season. Mass-market retailers, though, will be able to dream only of bottom lines just like the ones they used to know. That tracks the divergent paths in the broader economy between high-income Americans, who have held onto their jobs and reduced their debt over the last two grim years, and middle-class workers, who are anxious about job security and their tight household budgets. "The luxury consumer will be the stellar spender this holiday," says Michael P. Niemira, chief economist at the International Council of Shopping Centers. The **J.C. Penney**s and **Wal-Mart**s of the world will have to coax their customers to spend. "Our core customer's right in the middle, economically, so they're probably the most constrained," says J.C. Penney's chief marketing officer, Michael J. Boylson.

In an online survey conducted last month by BIGresearch, a Worthington (Ohio) research firm, respondents with household incomes of less than $50,000 said they'd spend an average of $490.33 this season, down 1.2 percent from last year. Those with household incomes of $50,000 or more said they'd spend 2.9 percent more than in 2009, an average of $942.12. Those results are in sync with ICSC forecasts that sales at luxury stores open more than a year will surge as much as 8 percent in November and December over a year ago, com- ➜













Illustrations by Peter Arkle

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’Tis the Season for Mixed Results

For some companies, the fourth quarter is cheery. For others, it’s no party.

Some that depend on the holidays...

Company	Industry Sector	% of profits made in Q4
Big Lots	Discount retail	70%
Sears	Retail	57%
Best Buy	Electronics retail	56%
Williams-Sonoma	Luxury retail	53%
TIBCO Software	IT services	49%
Weight Watchers	Weight loss	19%
Coca-Cola	Beverages	18%
Carnival	Travel	15%
Whole Foods	Food retail	14%
Campbell Soup	Food manufacturing	9%

...and some that don’t.

DATA: BLOOMBERG

pared with a 1.5 percent to 2.5 percent gain at discounters.

Coach, the largest U.S. maker of luxury leather goods, has increased its inventory by 36 percent, including its line of Sophia satchels that range from $298 to $1,000. **Nordstrom** is selling a $1,165 D&G sweater jacket for men and Gucci watches priced up to $1,345. “I just got out of a meeting about doing more in the designer business,” says Peter E. Nordstrom, the store’s merchandising president. “We think there is a lot more room for us to continue to layer on more. We’re bullish on it.”

The Italian jeweler **Pomellato** is broadening its assortment of hardware at the so-called low end ($2,000) and the high end ($100,000-plus). The company has been previewing its wares at Bergdorf Goodman. On display: a $51,790 bracelet encrusted with brown diamonds. For those with slightly less expensive tastes, the company offers the Nudo lineup of 10 rose gold rings, which retail for $1,990 apiece. “It’s an alternative to a very nice [hand]bag,” says Managing Director Andrea Petochi.

Leslie Dickstein, a Realtor who lives in Manhattan, plans to spend $7,000 to $10,000 on gifts for her fiancé, family, friends, and business contacts, up from $5,000 to $6,000 last year and $2,500 the year before. A rebounding equity market has lifted her spirits. “The stock market does affect my mood, because it affects everyone around me,” says Dickstein, whose clients hail largely from Wall Street. She’s in the market for luxury accessories and apparel—**Hermès**, **Gucci**, **Portolano**—and wine.



The goodies glisten less at mass-market merchants, which have been cutting prices early and often. Last month, **Best Buy** offered a free phone with two-year contracts, and it plans to keep the deals coming. The world’s largest seller of consumer gadgetry is spending more in marketing this season than last. **Family Dollar Stores** has been promoting its lineup of $5 toys. In early November, Mary Kirkman was scouting a Family Dollar store in Greensboro, N.C. Once she gets paid this month, she plans to buy a doll and tea set for her two-year-old granddaughter. “That’s all I can afford,” says Kirkman, who works in a tool factory and hasn’t had a raise in three years. This holiday, Kirkman plans to spend about $230 on her five grandkids, about the same as last year and a quarter of what she spent four years ago on laptops and gadgets.
—Chris Burritt and Cotten Timberlake, with Lauren Coleman-Lochner and Andrew Roberts

The bottom line *Luxury retailers are expected to thrive, while mass-market chains struggle, in what’s likely to be an uneven holiday shopping season.*

812

BILLION DOLLARS

Decline in U.S. consumer debt since its peak in September 2008, a drop of 6.5 percent. Total consumer debt was $11.7 trillion on June 30, 2010.

DATA: FEDERAL RESERVE BANK OF NEW YORK

Retailing

The Staying Power Of Pop-Ups

▶ A new wave of temporary stores peddle experiences, not goods

▶ “I’m more of a try-before-buy person, so this is good”

In late October, Rachel Petersen walked into a store on 57th Street in Manhattan down the block from pricey department store Bergdorf Goodman. She took in the neon lights and tinted windows and thought she’d stumbled into “a private event or something.” The 30-year-old administrative assistant soon discovered that she was at **Procter & Gamble**’s New York pop-up store. The 4,000-square-foot space had no cash registers because everything was free—including a full CoverGirl makeover or a Head & Shoulders wash and blow dry. Petersen tested some lotion and left with a Febreze scented candle. “I’m more of a try-before-buy person, so this is good,” she said.

The P&G store, which drew 14,000 visitors in the 10 days it was open, represents a new iteration in the evolution of the pop-up. The first generation of stores, which cropped up in the early part of the decade, were often little more than shelving and cash registers in empty mall space with a makeshift sign draped over the old tenant’s marquee. They opened for a month, then disappeared. Many retailers have since hopped on the trend and upgraded the format with more spending on in-store displays and fancy signage to blend in better with their mall neighbors. And while pop-ups can bloom in any season, the holidays remain an ideal time for temporary stores, given the heavy foot traffic.

With U.S. retail vacancy rates at the highest levels in a decade, there’s no shortage of space. **Toys ‘R’ Us**, for instance, boosted its number of holiday season pop-ups this year to 600, from 90 a year ago, and hired 10,000 workers to operate them. Many of the 4,000-square-foot locations are in malls that formerly housed KB Toys, a toy chain that liquidated last year. **Borders Group** has increased its pop-up

OPPOSITE PAGE, FROM TOP: TOM WILLIAMS/ROLL CALL/GETTY IMAGES; PHOTOGRAPH BY ALEX WELSH FOR BLOOMBERG BUSINESSWEEK

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The Tea Party queen wants some respect page 39 ▶





Levi's pop-up "workshop" in New York is drawing 3,000 visitors a week

count fivefold, to 25, most of them in malls where the bookseller used to have a presence.

Although pop-ups have moved up in the world, for some the term still has downmarket connotations. Nataraj Iyer, a P&G marketing executive, prefers "interactive experience." **Pierce Smartfusion,** the firm P&G hired to run the 57th Street experiment, describes itself as an "experiential" agency that tries to deepen the "conversation" with shoppers. With the P&G store, the goal was not to move merchandise but to build brand loyalty. "The woman getting her hair colored will remember this the rest of her life," says Christian Charapata, a pop-up veteran who managed the P&G store.

Levi Strauss also hopes to create a lasting impression with the "workshop" it opened last month at a former art gallery in Manhattan's SoHo district. The bright-white, 10,000-square-foot space is furnished with benches made from cargo pallets and focuses on the art of (pre-digital) photography. Visitors can rent vintage cameras and sign up for free classes. The theme extends the denim maker's gritty Go Forth advertising campaign, a celebration of craftsmanship and collaboration that features scenes of regular folk rebuilding a Rust Belt town. The company says the store has been drawing 3,000 visitors per week. The hope is that each will talk, text, and tweet about their experience. "Success is exposure," says Erik Joule, who runs men's merchandising, design, and licensing. Eventually, he hopes, people will say, "Wow, that's Levi's?"

Christina Norsig, a New-York based e-commerce entrepreneur, runs **Pop-Up Insider**, an outfit that brings together property owners and potential pop-up tenants. Norsig, who won't disclose clients' names, has listings in a handful of states, including Minnesota, Florida, and Maine, and plans to expand her geographic reach next year. "This whole notion of temporary retail is here to stay," she says. "It's going to be a marketing tool for retailers going forward, whether they are testing a neighborhood or marketing to the end consumer." —*Matt Townsend*

***The bottom line** Procter & Gamble and Levi Strauss are using pop-up stores to connect with customers and build their brands in new ways.*

HOLIDATA

Gift cards are tops on Santa's list this year, with 57 percent of respondents ranking them their No. 1 choice in a recent survey by the National Retail Federation. That's up from 55.2 percent the previous year. In 2009, Americans purchased an average of 3.5 gift cards each.



Marketing

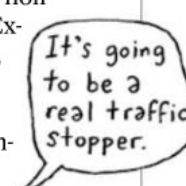
Holiday Windows: This Year the Fun Is Digital

▶ New York retailers use more high-tech displays to lure shoppers

▶ "Yes, Virginia, there is a [computer-generated] Santa Claus"

Starting on Nov. 22, giant snowflakes will dance with bubbles to the sound of bells and chimes on New York's Fifth Avenue, beamed by digital projectors onto the facade of **Saks**' flagship store. "It's going to be a real traffic stopper," says Saks' senior vice-president for marketing, Terron Schaefer, from his office overlooking St. Patrick's Cathedral. "We've warned the city." Saks' roughly two-minute production will run for six weeks. (Repeating every 13 minutes nightly, it's timed to avoid clashing with the tolling of the cathedral's bells.) That's longer than anyone has ever kept such a projection going, says Sean Reynolds, its co-creator and global creative director at marketing firm **Iris Worldwide**.

Saks is one of many New York stores enlisting **Spaeth Design** to help add some high-tech pizzazz to its holiday windows. Run by Chief Executive Officer David Spaeth, a mechanical and aeronautical engineer, the firm has been producing window wonderlands for four decades. Because it works with competing stores—this year, Saks, **Lord & Taylor**, and **Neiman Marcus**' Bergdorf Goodman are among its clients—each of its employees is required to sign a confidentiality agreement. Client visits to its 20,000-square-foot studio are staggered, and rivals' projects are covered with screens when customers arrive.



Until recently stores mostly used animated figures and a dollop of Santa Claus to draw holiday gawkers. Now more are turning to video to impress, says Sandy Spaeth, president of the family firm. Saks' projections will be accompanied by a 16-window tableau that includes two 3D video monitors that don't require the use of special glasses.

Last year shoppers could send letters to Santa using a touch-

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screen window in front of the 34th Street flagship **Macy's** and read live tweets in the Saks windows from tech-savvy fans of the store. This Christmas, Macy's is using LED screens to tell the "Yes, Virginia, There Is a Santa Claus" story, says Paul Olszewski, director of windows. Macy's Bloomingdale's unit is filling its Manhattan windows with 100 digital screens that play computer-generated animations of winter landscapes.



Bergdorf Goodman is staging a competition on its website that lets browsers create their own holiday window fantasy, using images tied to Bergdorf's 19th century vision of the future window theme. The winner will get a $2,500 gift card, and his or her creation will be displayed on social media sites and the store's blog. "Technology has made the final product more engaging and more fun for shoppers," says Alison Embrey Medina, executive editor of *DDI* magazine, which awards prizes to the best store windows in New York.

Not everyone is abandoning the old ways. Simon Doonan, creative director of **Barneys New York**, prefers to handcraft. For 2010, he's tapping into the cultural obsession with celebrity chefs such as Mario Batali and Rachael Ray, caricaturing them with his signature papier-mâché figures. "Technology can seem really cold at holiday time," Doonan says. "There is so much digital imagery in people's lives. Windows provide a break from that." —*Cotten Timberlake*

The bottom line *New York's big retailers are increasingly using high-tech window displays to lure shoppers during the holiday season.*

HOLIDATA

Up to 30 million live trees are sold in the U.S. each year, according to the National Christmas Tree Assn. The mean price of a live tree in 2009 was about $41. Oregon is the No. 1 producer. About 80 percent of all artificial trees are manufactured in China, according to the Commerce Dept.



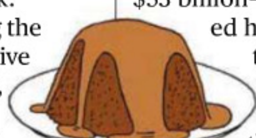
Food

In Britain, It's Feast Today And Fast Tomorrow

▸ U.K. supermarket chains expect shoppers to treat themselves

▸ "Christmas is a time when people trade up on food"

Budget cuts, tax hikes, rising unemployment–it's enough to make you lose your appetite. Not if you're British. As Britons brace for the austerity that will accompany Prime Minister David Cameron's campaign to wipe out the nation's record deficit, the U.K.'s top supermarket chains are betting that consumers will party this Christmas. Verdict Research is forecasting that this holiday season will be the best for U.K. retailers since 2007, with spending on food and grocery items climbing 3.5 percent, to $53 billion–39 percent of all projected holiday spending. "Despite the woes of the political economy, don't underestimate the propensity of the average British household to have a good time when Santa is in town," wrote Clive Black, an analyst at London brokerage Shore Capital Group in a recent note to clients.



J Sainsbury, the U.K.'s No. 3 supermarket chain, and rival **Wal-Mart Stores**' Asda, the No. 2, believe consumers will defy the downturn and add more expensive products to their shopping baskets as treats before the belt-tightening starts. On Jan. 4 the value-added tax levied on all prepared foods, including holiday goodies such as ice cream and salted nuts, will rise to 20 percent from 17.5 percent. "Christmas is a time where people trade up on food," says Sainsbury Chief Executive Officer Justin King. "We've seen people quite clearly manage their weekly spend so they can preserve things that are important to them."

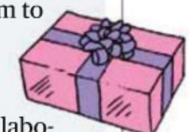
In preparation for the holidays, Asda and Sainsbury have bulked up their private-label offerings. "The U.K. consumer is always prepared to splash out at Christmas, and the own-brands are typically higher gross margin, so it's a clever strategy," says

➔32

Speed Dial Robert Burke

The luxury consultant and former fashion director at Bergdorf Goodman says reliable trumps trendy

How are luxury consumers different this holiday season?
They were more skittish last year. Retailers were looking for ways to drive traffic. That was their biggest concern. Now that traffic has started to pick up, they have to have a product that the customer feels is an investment and not a fleeting trend. That's the only way to get them to spend any significant money.



How do you do that?
With a heritage brand or a collaboration. We're seeing Timex reissue a classic men's watch for $150, or we're seeing Uggs and Jimmy Choo collaborate on a designer Ugg [boot]. They put a great deal of hardware and studs on them, and they're selling for $495 to $695. And it's a limited time. At the very high end, Hermès continues to increase their sales because the luxury consumer, instead of buying a trendy handbag or two, would rather splurge on something they are going to have for a long time.

Does that mean smaller inventory?
Yes. As opposed to [merchants] saying orange is the hot color or pink is the hot color and then owning a huge inventory you can't move, they're going with proven classics.

So, it's a very conservative market?
Yes, but the flip side is, if you're too conservative, you're not going to motivate people to part with their money.

Is there hope for brands that don't already have name recognition?
It's not impossible. You have to have a really outstanding product. It's become harder and harder. Those are brands that have gotten squeezed.

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Hope for the Holidays

Despite the uncertainty about consumer spending, many companies are making big bets for this holiday season.





Microsoft's Kinect videogame motion controller is its weapon to steal market share for its Xbox 360 from Nintendo's Wii. The $149.99 Kinect uses webcam technology and motion sensors so that characters can mimic players.

Best Buy will promote Samsung's 7-inch Galaxy Tab computer. It might be a hard sell since the Android-based tablet starts at $399, just a tad cheaper than Apple's 10-inch iPad.



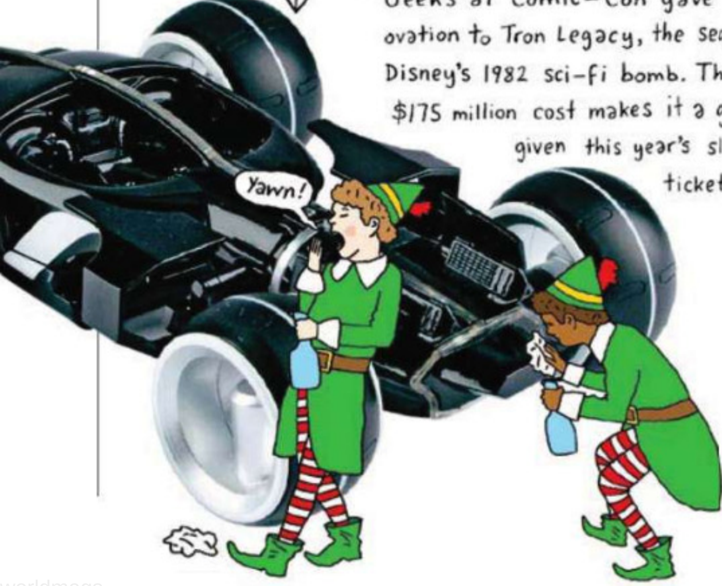
Retailer Dollar General will heavily promote $12 Bobbie Brooks women's jeans. The chain will price no item in that women's line above $16 this Christmas.



Coach thinks consumers are ready to spend. It's rolling out new products throughout the season, including a line of $298 to $1,000 Sophia bags.



Geeks at Comic-Con gave a standing ovation to Tron Legacy, the sequel to Tron, Disney's 1982 sci-fi bomb. The film's $175 million cost makes it a gamble given this year's sluggish ticket sales.

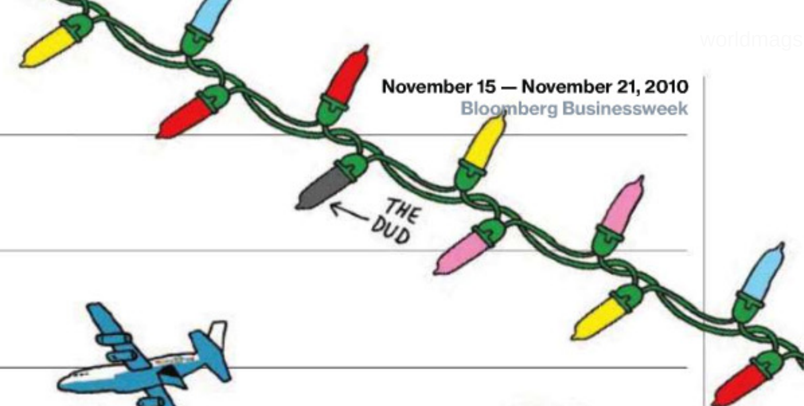


After higher-priced holiday baked goods drew disappointing sales last year, Wal-Mart's Sam's Club stores won't sell pies for more than $10 and cakes for more than $18.



TABLET: DAVID PAUL MORRIS/BLOOMBERG

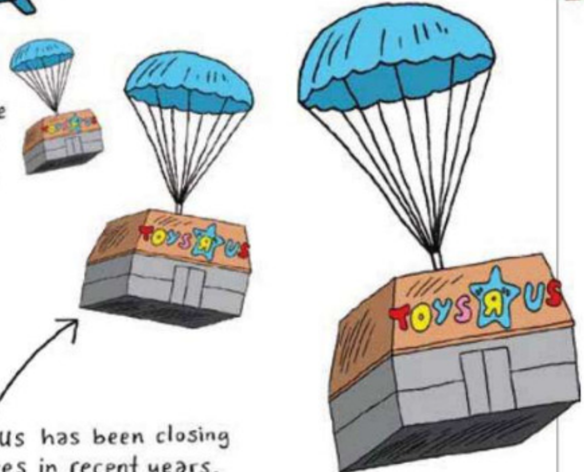
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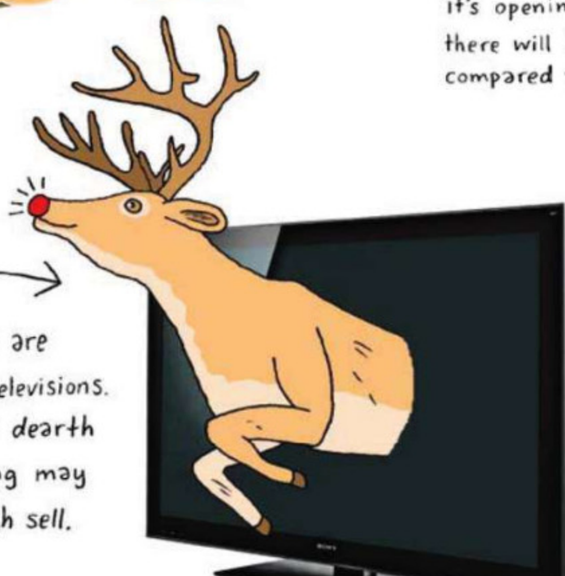


Last Christmas, retailers scrambled to offer $10 toys to recession-weary shoppers. This season, Toys 'R' Us and Wal-Mart are promoting more expensive playthings, such as Fisher-Price Imaginext's $100 BigFoot remote-controlled action figure.



While Toys 'R' Us has been closing permanent stores in recent years, it's opening more holiday pop-up stores. This year there will be 600 of these seasonal mushrooms, compared to 90 in 2009.





Sony and its rivals are betting big on 3D televisions. Steep prices and a dearth of 3D programming may make them a tough sell.

The Call of Duty videogame franchise has generated more than $3 billion in sales, so this month's rollout of Call of Duty: Black Ops isn't exactly a gamble. Still, publisher Activision says it will spend more on marketing the $59.99 title than it's ever spent hawking a game.







Coca-Cola is launching its first global Christmas ad campaign in 15 years. "Snow Globe" features an original song by rock group Train as Santa Clause sips a Coke and reunites lonely people (and a dog). Coke saves millions by running a single campaign in 90 countries.

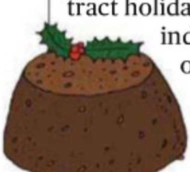
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Sam Hart, a retail analyst at Charles Stanley, a brokerage in London.

Sainsbury, for instance, is doubling its highest-priced "Taste the Difference" line of food, which typically accounts for about 5 percent of everything it sells. Among the approximately 300 additional items: a $4.80 tub of mince-pie ice cream and $8 cognac-laced Christmas pudding.

Asda is adding 140 products to its Extra Special premium line over the next six weeks, including sherry trifle gateaux, trout and horseradish terrine starters, and Christmas pudding aged for six months. Almost three-quarters of the purple-and-cream-branded items have been updated or changed to attract holiday shoppers. As a further inducement, the chain began offering up to 25 percent off the new premium products in October. "We try and keep customers with us when they trade up at Christmas," says Jo Johnson, brand manager for the Extra Special line. "We're getting customers to understand we have a truly premium range with the discounts."



Some merchants warn that the predictions may be too optimistic. **Wm Morrison Supermarkets** CEO Dalton Philips is less upbeat on the outlook, predicting a "tough" festive season. "People say the British are going go to have a great Christmas irrespective," of the economic backdrop, Philips says. "I'm not so sure." —*Sarah Shannon*

The bottom line *Retailers J Sainsbury and Asda are expanding their premium private-label offerings to lure holiday shoppers looking to treat themselves.*

Toys

For China's Toymakers, An Unwanted Gift

▸ The mainland's fast-appreciating yuan is hurting small toy factories

▸ "American consumers will have to pay more for their Christmas trees"



A stronger yuan is cutting into toymakers' already thin profit margins

IMAGINECHINA/AP PHOTO

Lucy Liang, a sales manager for **Jiangsu Zhongxin Toys**, disappointed potential U.S. and European clients who were inspecting pink and yellow teddy bears in the toymaker's stall at a trade fair in Canton last month. "My boss orders us to turn down all the orders for the good of the company" because China's yuan may rise, crimping profit margins, said Liang as she sipped pu-er tea in her stand. "Even first-class economists can't predict whether the yuan will appreciate or by how much. How could we?"

China's toymakers accept profits of as little as 3 percent to stay competitive. Such low margins, coupled with payment periods of three months or more, mean companies are particularly vulnerable to currency fluctuations, says Lin Songli, an analyst with Guosen Securities in Beijing. The yuan has gained 6.4 percent against the euro and 2.5 percent against the dollar so far this year. "If the yuan rises to 6 to the dollar, we're doomed," says Simon Pan, general manager of **Zhejiang Huangyan Hongfan Toys Factory**. The company is raising prices by 3 percent to 5 percent to offset the Chinese currency's gains, but further increases would mean losing customers, he said in an interview at his booth, which was filled with educational toys and brain-teasers destined for the U.S.

If the yuan rises to 6 to the dollar, we're doomed.

The pricing pressure could hurt in the U.S. "The prospect of a stronger yuan means American consumers will have to pay more for their Christmas trees and probably everything that is made in China starting 2011," Guosen's Lin said. Agrees Ben Cavender, an analyst at China Market Research Group: "If toymakers are forced to raise prices in order to compensate for a falling U.S. dollar—and to stay in business they will probably have to—it means higher prices for U.S. consumers in the coming holiday season."

China has held the yuan's rise to about 2 percent since a June pledge to introduce more flexibility, sparking criticism that China gives an unfair advantage to its exporters. Premier Wen Jiabao has said a rapid climb for the yuan would cause social and economic turmoil.

Some companies say they've already been pinched by the yuan's gains as clients from the U.S., Europe, and Japan continue to expect cheap prices when buying in China. "Since the government revalued the yuan, we have been declining long-term orders—anything beyond six months—because we might even lose money by then," says Lin Ying, a sales manager at Guangdong-based **Shantou Meichang Plastic Factory**, which makes plastic blocks and beach toys. "If the yuan keeps rising, life would certainly be even harder for us," she says.

Customers expect the same prices as last year, says Susie Ying,

HOLIDATA

If trends hold, champagne makers in France won't be toasting their U.S. sales this holiday season. From 2005 to 2010, consumption of French bubbly fell 16.8 percent stateside, according to Euromonitor International. During that time demand for other sparkling wine, such as Spanish Cava and Italian Prosecco, advanced 12.7 percent.



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general manager for **Shanghai Master Plastic Products**. The maker of pools and beach toys had to raise prices 15 percent, even as "most of our customers can only accept a 7 percent to 8 percent rise," Ying says. Her company is focusing on more expensive items because margins tend to be higher. "From the purchase orders we received, high-value toys have taken the lead on demand," says Karson Choi, executive director of **Early Light International**, a Hong Kong-based toymaker whose clients include **Mattel**.



Dalian Ponytoy, which sells rideable toy horses and zebras for $200, wholesale, says it's also hurt by gains in the Chinese currency. "Two months ago the dollar-yuan exchange rate was 6.8, now it's 6.65," says General Manager Tony Nie. "This has a huge impact on us. A few years ago the exchange rate was 8 yuan to the dollar."

Almost 70 percent of exporters project a decrease in orders if the yuan strengthens by an additional 2 percent against the U.S. dollar, according to a survey of 239 Chinese suppliers by Global Sources, which matches buyers and sellers of manufactured goods. "Many companies, particularly those in labor-intensive industries [like contract toymaking], are running on paper-thin margins and have no room to absorb currency-exchange losses," says Craig Pepples, Global Sources' chief operating officer. In contrast, Mattel, the world's largest toy company, posted a profit margin of 9.7 percent last year, while No. 2 **Hasbro** had 9.2 percent, according to data compiled by Bloomberg.

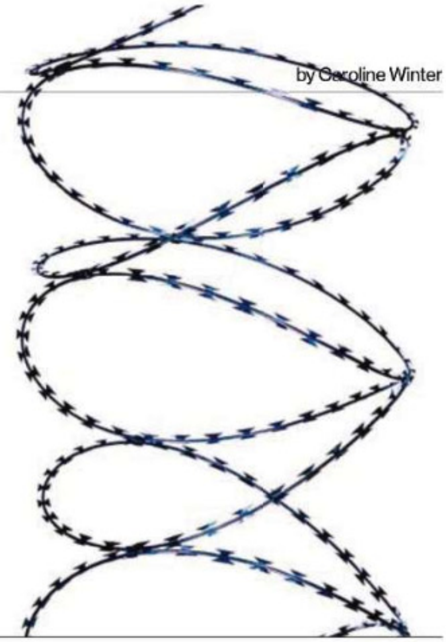
Zhejiang Sunny Import & Export, which sells wooden blocks that can be rearranged to resemble vehicles and robots, has tried to hedge against currency losses. It billed in euros, then lost money when the currency dropped against the yuan, says manager Liam Zhu. "We changed back to the U.S. dollar, but now the U.S. dollar is fluctuating and the renminbi [another term for yuan] is still appreciating," says Zhu. B

—Michael Wei and Stephen Engle

The bottom line *The appreciation of China's currency is squeezing its small toy manufacturers, which already operate on tight profit margins.*

Briefs

by Caroline Winter



Tyco International
Biding time in hope of better markets

Tyco International, the world's largest maker of security systems, agreed to sell a majority stake in its electrical and metal products unit to buyout firm Clayton Dubilier & Rice for $720 million, withdrawing plans to spin off the division. Proceeds from the sale of the 51 percent stake will go toward accelerating share buybacks under a $1 billion program announced on Sept. 8. The unit, which will operate as a standalone entity called Atkore International, makes items such as barbed razor ribbon and metal-clad electrical cables and had revenues of $1.4 billion in 2009. The decision to divest means Tyco could profit more by selling the remaining 49 percent when markets improve.

Google
Fatter paychecks for all



In a bid to retain talent, Google plans to give 10 percent raises to all of the company's 23,000 employees worldwide, *The Wall Street Journal* reports, citing an e-mail from Chief Executive Officer Eric Schmidt. The increases will take effect in January. Googlers have been decamping to Facebook and other Silicon Valley outfits in increasing numbers. The company posted strong third-quarter results, but the across-the-board pay hike may heighten investor concerns over expenses.

General Electric
$2 billion—and 1,000 jobs—in China

General Electric says it plans to invest more than $2 billion in China, creating 1,000 jobs in the country. The investments include $1.5 billion in joint ventures with Chinese state-owned tech companies and roughly $500 million for product development and a half-dozen innovation centers. GE named Chengdu, Shenyang, and Xian as possible locations for the centers. CEO Jeffrey Immelt is targeting China and India because they will likely lead global growth in energy demand. GE rival Siemens, meanwhile, is close to signing a contract to supply a still-to-be-named Chinese city with electric-vehicle charging infrastructure. The chargers will be installed in the next three months, Siemens says.

Eli Lilly
Investing in disease diagnostics

$300
MILLION

Eli Lilly agreed to buy Avid Radiopharmaceuticals for $300 million. The deal gives Lilly Avid's molecular imaging agent, florbetapir, which is thought to detect amyloid plaque, a substance scientists suspect is the main cause of Alzheimer's disease. Avid is also developing diagnostic compounds for Parkinson's disease and diabetes. All shares of closely held Avid will be acquired, and Avid stockholders will be eligible for as much as $500 million in additional payments, according to Lilly.

E.ON
U.K. grid assets in play?

German utility E.ON is considering the sale of its U.K. electricity grid to help weather a slump in natural gas prices and to pay for a planned German tax on nuclear power stations, people familiar with the matter say. London's *Sunday Times* reports that E.ON is in advanced talks to sell the network for up to $5.7 billion to Abu Dhabi Investment Authority, Canada Pension Plan Investment Board, and Macquarie Group.



On the Move

Northern Rock CEO Gary Hoffman to step down • **New England Sports Ventures** Spencer Stuart retained to find a CEO for Liverpool soccer club • **News Corp.** Ex-CNN anchor Lou Dobbs to host program on Fox Business

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Contents ▶ Michele Bachmann's quest for respect 39 ▶ Tim Geithner is long on yoga 40 ▶ The shrinking world of Nancy Pelosi 40 ▶ The bailout cop the White House loathes 42 ▶ The congressional lame-duck agenda 42 ● Edited by Paula Dwyer

The Valedictorian's Dilemma

▶ **High-achieving undocumented students look to Harry Reid for help**

▶ **"All of them have seen graduation as the hardest thing they've ever had to do"**

When Mirta Gonzalez was accepted to Harvard in 2004, her relief was mixed with trepidation. As an undocumented immigrant, she feared her Mexican passport would raise suspicion on the trip to Boston from her California home. Gonzalez had never admitted her alien status—not to high school counselors, not even to Harvard—and had no one to turn to for logistics help. "In a way, getting in wasn't the hardest part," she says. "It was getting there."

Gonzalez, whose name has been changed to protect her identity, made it across the country undetected and enrolled. No one at Harvard asked about her status. It wasn't until her senior year that she searched out other undocumented Ivy League students to see how they planned to cope with the barriers to entering the professional world. As it turned out, there were more than she'd expected. In Harvard's 2009-2013 classes, she says she found at least 18. She located similar numbers at Yale and a handful at Cornell and Brown. "I was amazed by how many I found," says Gonzalez.

Ivy League schools offer their own version of "don't ask, don't tell" and have become sanctuaries for a select—and possibly growing—group of high-achieving illegal immigrants who are able to defer the harsh realities of undocumented life, at least until graduation. Soon, U.S. Senate Majority Leader Harry Reid, who owes his reelection largely to Nevada's Hispanic voters, will try to make it possible for many of those students to stay in the U.S. legally.

Reid pledged in an Oct. 31 Univision interview to bring to a floor vote the Development, Relief and Education for Alien Minors, or Dream, Act in the lame-duck session beginning Nov. 15. The measure would allow students who arrived in the U.S. before age 16, have



Pedroza, who may be deported, hopes to finish at Cornell

PHOTOGRAPH BY JASON REBLANDO FOR BLOOMBERG BUSINESSWEEK

been in the country at least five years, and have a high school or equivalent degree, to apply for permanent residency after two years of college or military service. The legislation failed in September when Reid sought to attach it to a $726 billion defense authorization bill. The election-eve vow to resurrect the proposal may have saved his career: Exit polls by Latino Decisions, a nonpartisan research group, show that 10 percent of votes cast in his Senate race were by Latinos. Of those, 90 percent backed Reid.

Of the estimated 11 million illegal immigrants in the U.S. today, about 65,000 complete high school each year, according to the Urban Institute. Of those, about 5 percent to 10 percent go to college. The Migration Policy Institute, a nonpartisan think tank, estimates that less than half of 2.1 million eligible youth would meet the act's requirements.

For students in the U.S. illegally, the soaring cost of tuition is a near-insurmountable barrier. They are ineligible for federal loans and, in most cases, in-state tuition. For those accomplished enough to make it to Harvard, Yale, Princeton, or Dartmouth, admission means a full ride—tuition, fees, room, and board—if they are needy. Some non-Ivies, including Amherst College and Massachusetts Institute of Technology, have similar policies. Brown and Cornell offer full rides for needy U.S. students only, but often help non-U.S. students, too.

In applying to college, Gonzalez says she "took that Princeton Review catalog they send you in the mail and just went through it, tearing out all the need-blind schools." She narrowed her list from there. To be as honest as possible, she applied as a foreign student and never addressed the fact that her transcripts and recommendations were from a California high school.

Others apply without noting citizenship (most applications don't require Social Security numbers). Some even admit their status. Colleges have no legal obligation to ask about immigration status, as long as no federal money is at play, and many turn a blind eye. "There is no citizenship requirement at Harvard," Jeff A. Neal, a Harvard spokesman, says in an e-mail. Some schools, such as Vassar College and Santa Ana (Calif.) College, openly say they offer aid for undocumented students. The Ivies and other elite schools appear to be the most attractive option. A June 2010 National Association for College Admissions Counseling (NACAC) study shows that schools admitting 50 percent of applicants or less are almost twice as likely to receive applications from undocumented students as those admitting more than 85 percent.

Reliable statistics for undocumented immigrants are hard to come by. It's impossible to know how their academic performance has changed over time. Certainly, more students are speaking up: David Hawkins, NACAC's director of public policy and research, says a growing number of valedictorians out themselves at the annual immigration rights rally in Washington, risking arrest. "Five or six years ago, one or two people [would] get up and say, 'I'm the valedictorian of my class,'" he says. "Now you'll see 10 or 15 up on stage." The Dream Act is behind much of the activism.



Reid, who largely owes his reelection to Hispanics, wants to help illegal students stay in the U.S.

One who might benefit is Pedro Pedroza, a Cornell University would-be senior whose sister graduated from Harvard in 2004, earned two master's degrees, and became a resident by way of marriage. Pedroza, who hopes to become a teacher, was detained in 2008 while traveling to Cornell from Chicago on a Greyhound bus. He had encountered U.S. Immigration and Customs Enforcement (ICE) agents on previous bus trips; they waived him on after seeing his Mexican documents and college ID. Not this time. Pedroza is now living with his parents in Chicago and awaiting a deportation hearing.

Dream Act proponents say young immigrants should have a chance to obtain legal status, especially since the U.S. faces a shortage of skilled professionals. They would generate between $1.38 trillion and $3.6 trillion over their work lives, estimates the North American Integration and Development Center, a research group at the University of California in Los Angeles. Opponents say the act would spur more illegal immigration. In the past, Democrats overwhelmingly backed the act; some Republicans did, too. Senator Richard G. Lugar (R-Ind.) is a co-sponsor. Senator Robert F. Bennett (R-Utah), who lost his reelection, has said he would vote for it as a standalone bill.

Bachmann showed a knack for fundraising in the midterms ...



Gonzalez, meanwhile, is navigating the complications of applying to medical school. Her undocumented classmates have left Harvard. Four of them, like Pedroza's sister, have enrolled in graduate programs. Two couldn't find legal employment in the U.S. and left the country, knowing that U.S. law requires them to wait 10 years before applying to return. "The world that Harvard provides is so privileged, and when you're thrown out without any ability to use the education you are provided, it's overwhelming," Gonzalez says. "I think all of them have seen graduation as the hardest thing they've ever had to do."
—*Caroline Winter, with Laura Litvan*

The bottom line *Even an Ivy League degree won't help undocumented students after graduation; Senator Reid vows to try to fix that in the lame-duck session.*

CLOCKWISE FROM TOP LEFT: JOSHUA ROBERTS/GETTY IMAGES; JASON ANDREW/GETTY IMAGES; ETHAN MILLER/GETTY IMAGES





... and her rhetoric resonates with Tea Party supporters

House Republicans

The Tea Party Queen Demands Respect

▶ Michele Bachmann seeks a House GOP leadership post

▶ "She's less likely to ... ask us to go along with the leadership"

House Republicans had just trounced Democrats in the midterm elections, and Representative Michele Bachmann was already at it again. The Minnesota Republican said in a Nov. 3 CNN interview that President Barack Obama's 10-day trip to Asia was costing taxpayers $200 million a day, an example of "over-the-top spending." It was the kind of shoot-from-the-mouth statement that has made Bachmann, a tax lawyer, anti-abortion activist, and Tea Party Caucus founder, famous—and her fellow Republicans cringe.

Now she wants respect. Bachmann is running for chairman of the House Republican Conference, the No. 4 leadership position. "I think my very strong clear voice has lent confidence to the Tea Party movement, and I think they've been vindicated" by the Nov. 2 elections, Bachmann says. In challenging Representative Jeb Hensarling, a four-term fiscal conservative from Texas, she takes on a popular member of the GOP Establishment who even Bachmann concedes is likely to win.

Still, her stock is up. The Tea Party Caucus, now at 53 members, could swell to more than 80 when 28 or so Tea Party-backed freshmen arrive in January. By comparison, the fiscally moderate Blue Dog Democrats were more than halved, dropping to just 25 members from 53. The Congressional Black Caucus, another powerful coalition, has 39 members. Bachmann, 54, from the Twin City suburbs, proved she has fundraising skills, too: She raised $11 million for her campaign, more than the likely new House Speaker, John Boehner of Ohio.

It remains to be seen if the Tea Party Caucus, which has met only a few times since its July founding, will be a real force. Congress has dozens of caucuses—there's one for wine lovers and one for biking enthusiasts—that rarely meet and don't have the ability to influence votes. One of Bachmann's supporters says she will help insulate newcomers from pressure from the Republican Establishment. "She's less likely to come back to us and ask us to go along with the leadership," says Representative Steve King of Iowa. "The conscience of a conservative will always be there at their shoulder."

Her divisive style makes some Republicans nervous. "She's a renegade," says Larry Jacobs, a University of Minnesota political science professor. "And she's made pretty plain that you can't trust the Republican leadership." Bachmann is prone to politically incorrect and sometimes inaccurate statements. She labeled the auto bailouts "gangster government" and said the Group of 20 nations was "one short step" away from "one world government." As for Obama's Asia trip, White House officials won't release the price tag, citing security concerns. But it likely falls far short of $200 million a day, according to PolitiFact.com, a *St. Petersburg Times* fact-checking service. A March 2000 trip to India and Pakistan by President Bill Clinton, at the time considered one of the most expensive Presidential forays in history, was estimated by the *Air Force Times* to cost about $10 million a day. —*Lisa Lerer*

53

Current number of Tea Party Caucus members

81

Potential size of Tea Party Caucus in January

The bottom line *Michele Bachmann's Tea Party Caucus could exceed 80 members next year, handing her influence over a powerful voting bloc.*

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Disclosure

The Geithner Family Seeks Investing Nirvana

▸ The Treasury Secretary owns stock in yoga retailer Lululemon

▸ Yoga wisdom: "Friends are more important than money"

Government officials often avoid conflicts between professional obligations and personal finances by divesting company stocks from their portfolios. So it comes as a surprise that, along with the standard mutual funds, Treasury Secretary Timothy Geithner owns a small amount of stock in yoga clothing retailer **Lululemon**.

The Vancouver (B.C.)-based company has attained almost cultlike status with urban women who carry Lululemon's reusable tote bags and assume the lotus position in its pricey workout clothes. The store sells, for example, the $58 "Ta Ta Tamer" sports bra and the $98 "Groove" pants. The Treasury Secretary, a runner and basketball player, has never been known for wearing spandex.

Turns out, he purchased less than $1,000 worth of shares a few years ago to teach his two children about the stock market, press aide Steve Adamske says. Geithner picked the company partly because of his now college-age daughter's interest in yoga—and as a hedge against her frequent Lululemon purchases, Adamske says. Additionally, Geithner owns $1,000 to $15,000 worth of **IBM** stock, which he inherited. (Disclosure forms give values in broad ranges only.)

The Geithners have potential as stockpickers: Since Lululemon's July 2007 initial public offering, the company has posted a 165 percent return. The Standard & Poor's 500-stock index, meanwhile, lost 20 percent in the same period. Still, it hasn't been an easy few years for the retailer, whose share price has fluctuated since the purchase, providing fodder for the family lesson plan.

Like most high-end retailers, Lululemon was hit by the financial crisis and the slowdown in consumer spending. The company's stock trailed the S&P from September 2008 to September 2009, when it took off. This year it's up 59 percent. Says Edward Yruma, an analyst at KeyBanc Capital Markets in New York: "This is good stock to own."



A Lululemon yoga block

Geithner might want to incorporate some of Lululemon's quirky culture into the kids' lessons. Emblazoned across its shopping bags are manifestos like: "Friends are more important than money." Here's one the chief U.S. economic policymaker may want to avoid: "Do one thing a day that scares you." —*Robert Schmidt*

The bottom line *Treasury Secretary Geithner is using an investment in a yoga clothier to teach his kids about the stock market.*

House Democrats

Nancy Pelosi Gets Downsized

▸ The Speaker faces a loss of power, perks, and privileges in January

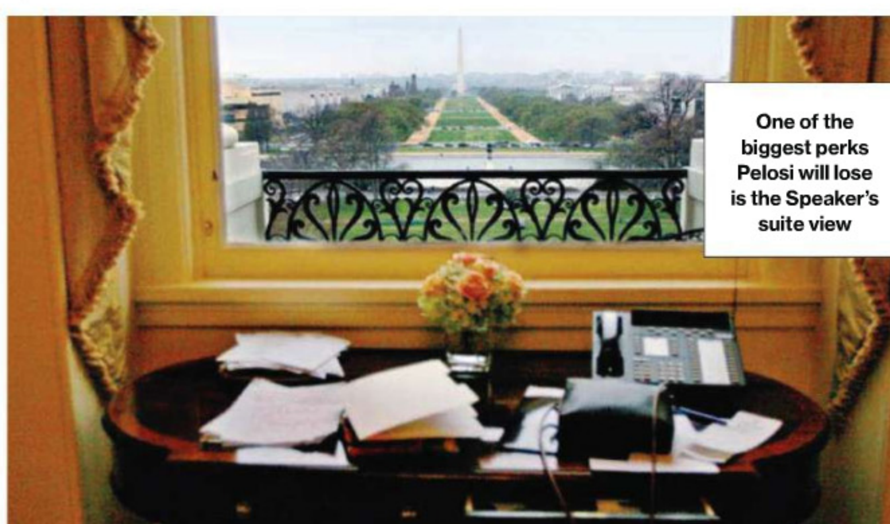
▸ "It's a profoundly humbling experience"

When Speaker Nancy Pelosi returns to the Capitol in January, she'll likely continue as House Democratic leader. Her loss of power as Republicans assume control of the House will be accompanied by an almost Dickensian reduction of circumstances—by Washington standards, anyway. Gone will be the spacious office suite with its federalist decor, the rides home aboard a military plane, and a good chunk of her staff. "It's a profoundly humbling experience," says Ross Baker, a Rutgers University political scientist.

Pelosi seemed to enjoy the perks that came with a job that made her second in line for the Presidency. Soon after becoming Speaker in 2007, she secured use of a military aircraft for nonstop travel between Washington and her San Francisco home. She banned smoking in the Speaker's Lobby, an ornate room next to the House chamber where members gather between votes.

As she prepares to swap jobs with House Minority Leader John Boehner (R-Ohio), she'll lose the right to authorize overseas congressional trips and dole out prime office space to lawmakers. She will also shed 10 percent of her $5.1 million office budget and lose nearly half of what records show is a staff of over 50. A Capitol Police security detail will still shuttle her around Washington in an SUV, but she'll have to go back to flying commercial. Nadeam Elshami, Pelosi's deputy communications director, says the Speaker doesn't care about any of that: "This job is not about the size of the office, it is about America's middle class."

The biggest change will be her workspace. The Speaker's suite of offices adjacent to the Capitol rotunda is rich in history and architectural detail, such as decorative mantels and murals. A balcony provides an unobstructed look down the National Mall—one of Washington's finest views. Artifacts in a separate ceremonial office include a tall case clock and


One of the biggest perks Pelosi will lose is the Speaker's suite view

LOIS RAIMONDO/THE WASHINGTON POST/GETTY IMAGES

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a Federal Period sideboard donated by a family that once lived near George Washington. The Minority Leader's suite, by contrast, was added in 1959. Its view is of the Library of Congress. The suite comes with a conference room and two staff offices; other aides work in windowless quarters a floor below.

Only three of the 52 House Speakers later served as Minority Leader. The last time was in the 1940s and '50s, when Democratic Leader Samuel T. Rayburn and Republican Joseph William Martin Jr. repeatedly swapped offices as power shifted. After 1954 elections that would have returned Rayburn to the Speaker's suite, he told Martin to stay put. The offices stayed with the Minority Leader until Newt Gingrich reclaimed them in 1995. While Boehner has no plans to pull a Rayburn, he does plan to keep Pelosi's smoking ban—and to fly home on commercial planes. —*Laura Litvan*

The bottom line *House Speaker Pelosi, who is likely to remain House Democratic leader next year, is about to see her Capitol lifestyle downsized.*

Treasury

A Bailout Cop Trains Fire on the White House

▶ The Administration is in open warfare with its bailout overseer

▶ "My job is not to go along with some script others have written"

The Troubled Asset Relief Program is shutting down, and the Treasury Dept. projects the $700 billion rescue effort will cost taxpayers less than $50 billion. So why is Neil M. Barofsky, the program's Special Inspector General, so unhappy?

The blunt-talking bailout cop is still hiring investigators and intends to keep his office open 8 to 10 years more. He employs 140 and has opened four more U.S. offices to probe fraud cases. "TARP being over is spin," he says.

None of this amuses the White House, which lambasted Barofsky, a former



"TARP being over is spin," says Barofsky, who is still hiring investigators

CLOCKWISE FROM TOP RIGHT: JONATHAN ROBERT WILLIS; GETTY IMAGES (2); BRAD TRENT

Congress

Lame Ducks Flock Back to Washington

Literally, a lame duck is a wounded animal unable to keep up with the flock, making it a predator's target. That's an apt description of the 49 defeated and 20 retiring House Democrats coming back to Washington on Nov. 15. Also returning will be three defeated and four retiring Democratic senators, along with six departing Republican senators, five of whom are retiring and one who was defeated. On their agenda: a slew of tax and spending issues,

ISSUE:
Bush-Era Tax Cuts

DEADLINE: **Dec. 31** | ONE-YEAR COST: **$207 bn**

The Conundrum
Congress must act to prevent higher income tax rates from taking effect Jan. 1. President Barack Obama wants to extend relief only on the first $250,000 of income. Republicans, fresh from a midterm electoral victory, want the cuts extended for all incomes.

The Outlook
Short-term extension, with a higher income cutoff of $500,000 or $1 million, is possible. So is gridlock, resulting in the tax cuts' expiration.

ISSUE:
Estate Taxes

DEADLINE: **Dec. 31** | ONE-YEAR COST: **$18 bn**

The Conundrum:
The estate tax, now at zero, returns in 2011 at a top 55 percent rate. It would apply after a $1 million tax-free allowance ($2 million for couples). Obama wants the exemption to be $3.5 million, and a 45 percent tax rate beyond that. Republicans want to repeal the tax.

Outlook:
Obama's plan would return the tax to 2009 levels. Republicans want to continue the rate at zero, but that would cost $69 billion. A compromise, backed by Senate Minority Leader Mitch McConnell, would set the rate at 35 percent and exempt the first $10 million, but it too would have to be offset with spending cuts or tax increases.

ISSUE:
Dividends and Capital Gains

DEADLINE: **Dec. 31** | ONE-YEAR COST: **$13 bn**

The Conundrum:
The 15 percent capital gains tax rate is scheduled to increase to 20 percent in 2011. Dividends would be taxed at a taxpayer's top marginal rate. Obama would preserve the 15 percent rate on both investment income sources for couples earning under $250,000. Republicans want the 15 percent rates with no income threshold.

Outlook:
The income thresholds and the extension period for these tax rates are likely to follow whatever compromise is negotiated on the Bush-era tax cuts.



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Putting the heat on OnStar
page 49 ▶



federal prosecutor from New York, on its blog last month. The missive, from Deputy Communications Director Jen Psaki, accused him of trying to "grab a few cheap headlines" by disputing Treasury's October estimate that the rescue of insurer **American International Group** would cost $5 billion, a huge drop from the $45 billion projected in March.

Barofsky says Treasury was playing with numbers when it changed how it valued its AIG holdings. Treasury says the numbers are based on the government's new plan to exit its AIG investment by converting its stake, now in preferred stock, to common. Psaki said Treasury used AIG's common price because preferred stock doesn't trade. The new estimate is realistic, she blogged, and "some people just don't like movies with happy endings."

Treasury is "just manipulating numbers for a big PR push," Barofsky told Bloomberg TV. He later called Psaki's posting "staggeringly inappropriate."

Inspectors general are rarely popular, but the animus toward Barofsky is intense. It started when he arrived in December 2008 and said his office in Treasury's basement reeked of sewage. (He moved to another building, keeping a coveted parking space at Treasury's main office next to the White House.) Then snippets of budget requests from Barofsky, who had sought law enforcement authority from Congress, turned up in the media. They showed he had spent thousands of dollars on ammunition and personal armor for some of his agents, feeding talk that he considered himself a modern-day Eliot Ness. The office's total 2011 budget request was $54.6 million.

He notes that his agents have raided two banks with the FBI and helped arrest the former chairman of a mortgage company. "We arrest people," he says. "That's really grasping at straws if they are trying to criticize us for being a law enforcement agency."

That's not how Treasury sees it. Barofsky feeds critics like Representative Darrell Issa (R-Calif.), who is set to head the House Oversight and Government Reform Committee, one former Treasury official says. Suddenly, hearings are scheduled, charges fly, and the media "eats it up, regardless of truth," says Andrew Williams, a former Treasury spokesman. Barofsky, he says, is part of the "cottage industry that has grown up around taking cheap shots at Treasury's efforts to avoid a total economic meltdown." Barofsky, a lifelong Democrat, says: "My job is not to go along with some script that others have written that has a beautiful, perfect ending." Ⓑ *—Robert Schmidt*

The bottom line *The war of words between Treasury and the Special Inspector General for TARP has turned nasty.*

6.2

Millions of people who have been out of work for six months or more

each with a pressing deadline. Will the lame ducks feel freed from the political fallout of the next roll call to vote their consciences? Will House Speaker Nancy Pelosi bring up measures she can't win, just to get Republicans on the record on difficult votes before she loses control? "She's got a brief window of opportunity," says University of Oklahoma political scientist Ron Peters, "to start the 2012 campaign." *—James Rowley and Ryan J. Donmoyer*

ISSUE:
Alternative Minimum Tax

EXPIRED:	ONE-YEAR COST:
End of 2009	**$66 bn**

The Conundrum:
The AMT hasn't been indexed for inflation since 2009. A tax increase affecting 30 million households already is on the books for 2010 unless Congress rolls it back. The cost for 2011 would be similar.

Outlook:
Of all the tax issues confronting lawmakers and the White House in the lame-duck session, enacting an inflation "patch" covering 2010 is the most likely outcome.

ISSUE:
Spending Bills

DEADLINE:	ONE-YEAR COST (EST.):
Dec. 3	**$1.4 tn**

The Conundrum:
Congress failed to complete any of the 12 annual appropriations bills before the Oct. 1 start of the 2011 fiscal year and has been funding the government with a series of stopgap measures. The latest temporary extension, which funds all government programs, except for entitlements like Medicare, Medicaid, and Social Security, at fiscal 2010 levels, expires Dec. 3. The cost per month is about $117 billion.

Outlook:
Another stopgap vote could push the issue into next year, when it might coincide with the government hitting the $14.3 trillion debt ceiling. That would put fiscal hawks and Tea Party lawmakers on the spot.

ISSUE:
Jobless Benefits

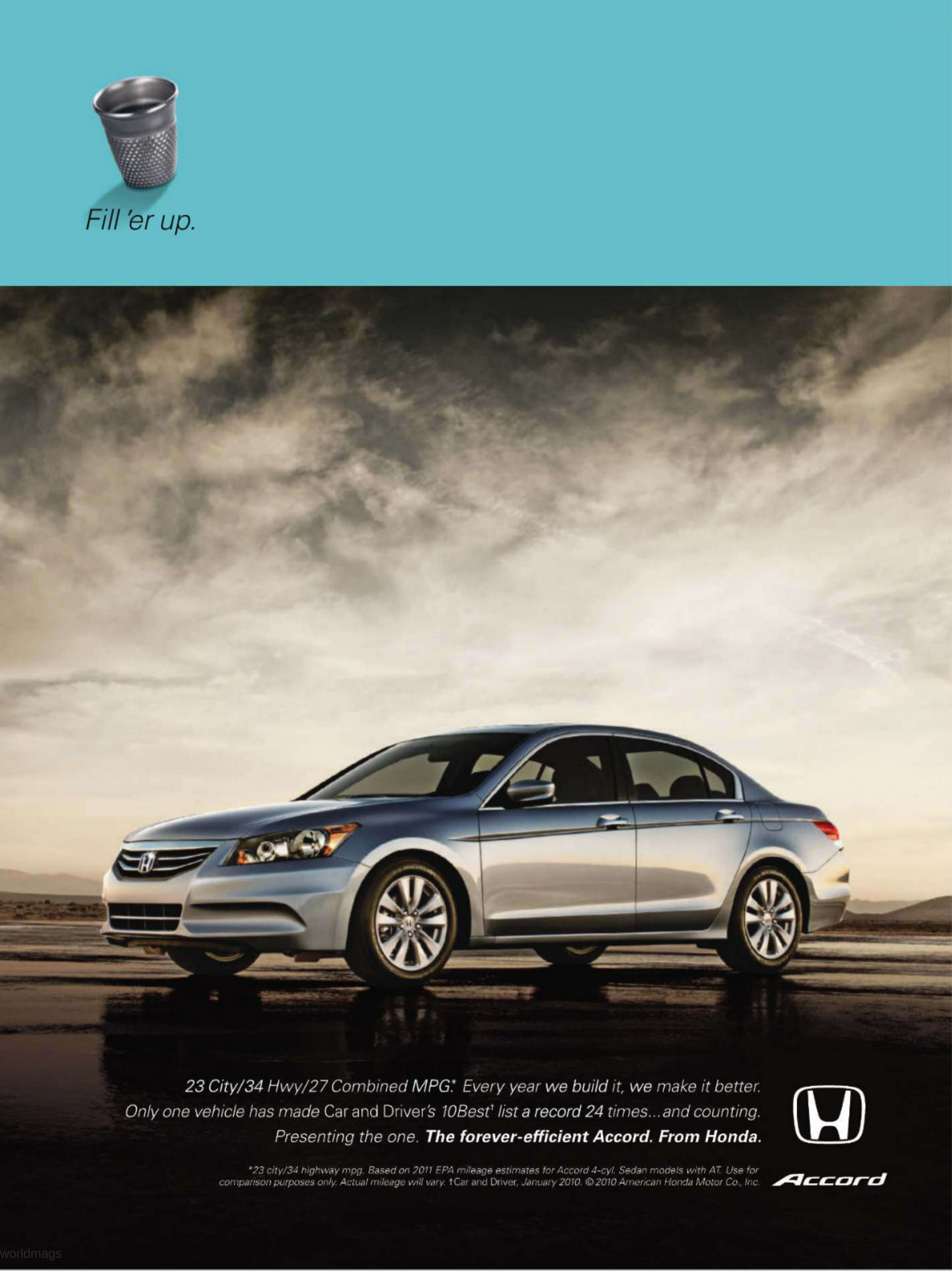
DEADLINE:	ONE-YEAR COST:
Nov. 30	**$65 bn**

The Conundrum:
At the end of November, about 2 million unemployed Americans will lose benefits. They are among some 6.2 million who have been out of work for more than six months. Some have received jobless benefits for as many as 99 weeks.

Outlook:
Democrats were already under pressure before the election to let federal jobless aid lapse, and the midterm election results only amplify that. Now the latest extension lapses just weeks before Christmas.



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Accord
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Technology

Nice Phone. Shame If It Got Hurt

▶ **Asurion quietly insures the handsets of more than 100 million cell phone owners globally**

▶ **"We think it's worthless," a consumer advocate says about mobile phone insurance**

Verizon Wireless calls its mobile phone insurance program Total Equipment Coverage. **Sprint Nextel** has Total Equipment Protection. **T-Mobile USA**: Premium Handset Protection. The names are barely distinguishable, and the insurance all comes from the same place: **Asurion**, a 16-year-old company in Nashville that would prefer you never heard of it.

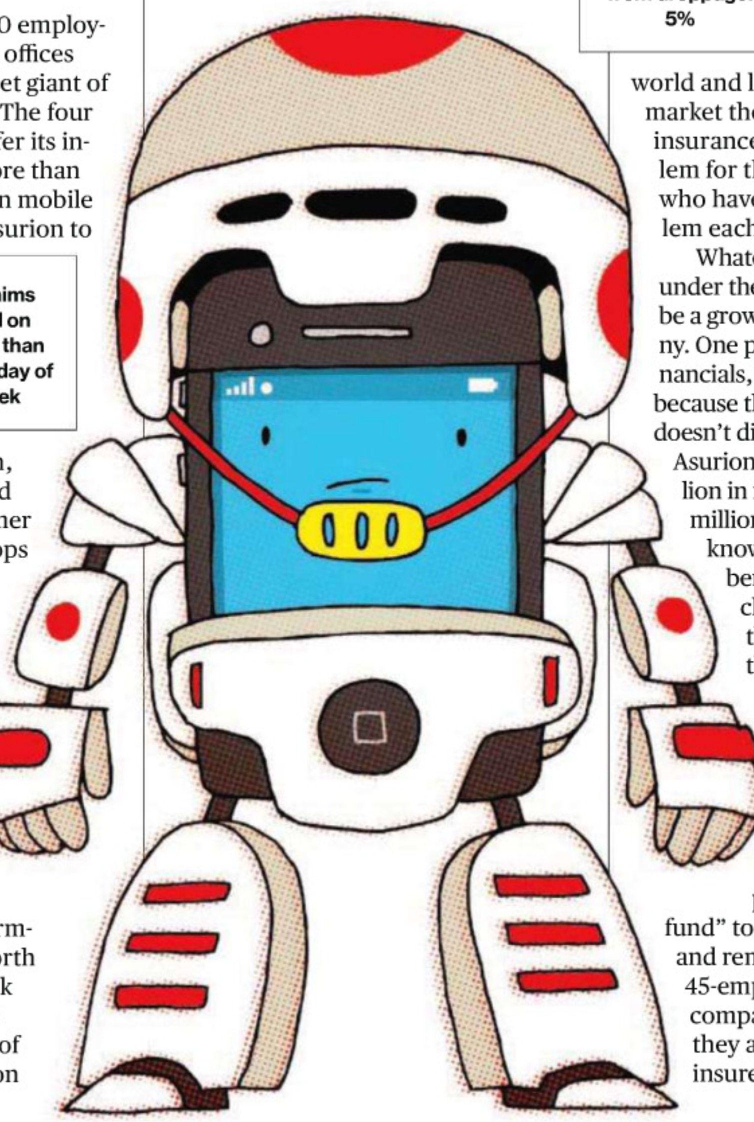
Asurion, which has 5,000 employees in more than two dozen offices around the world, is the quiet giant of the mobile phone industry. The four top U.S. wireless carriers offer its insurance exclusively, and more than 20 percent of the 293 million mobile customers in the U.S. pay Asurion to protect their handsets, according to the company. Asurion charges policyholders between $5 and $12 a month, depending on the model and type of coverage. If a customer loses a phone, breaks it, drops it in the toilet, or renders it unusable in any way, Asurion will try to ship a replacement in a single day—after the person pays a deductible.

More claims are filed on Mondays than any other day of the week

Some accident-prone owners—and parents of phone-toting kids—praise the sense of security Asurion provides. Consumer advocates, though, almost uniformly say the insurance isn't worth the extra expense. "We think it's worthless," says Michael Shames, executive director of the Utility Consumers' Action Network. *Consumer Reports* magazine advises cell phone shoppers to skip the coverage and hang on to their old phones as a backup should the new hardware meet its demise.

Asurion disagrees with those opinions, of course, but just getting the company to pipe up in its own defense isn't easy. "We like anonymity. We don't think publicity is generally a great thing," says its chief executive officer, Kevin Taweel, who starts an interview by asking a reporter to forgo a story on Asurion altogether. Taweel believes Asurion should stay out of the news because it merely "white labels" its product, selling insurance through 18 wireless carriers around the world and letting them rename and market the service. He adds that the insurance solves a significant problem for the one in four consumers who have some kind of phone problem each year.

Share of claims due to cracked housing, usually from droppage: 5%



Whatever its reason for staying under the radar, Asurion appears to be a growing and profitable company. One person familiar with its financials, who asked for anonymity because the privately held company doesn't disclose revenue or profit, says Asurion is on track to make $3.8 billion in revenue this year and $98 million in profit. Another person knowledgeable about the numbers says Asurion's profit, excluding interest payments to the three private equity firms that own it, is actually about half a billion dollars.

Taweel co-founded the operation that became Asurion in 1995 along with Jim Ellis, a fellow graduate of Stanford Business School. The pair had raised a "search fund" to seek out a company to buy and remake. They first acquired a 45-employee roadside assistance company for $8 million. In 1999 they acquired a cell phone insurer called Merrimac

ILLUSTRATION BY ALEX EBEN MEYER; DATA: ASURION

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Technology

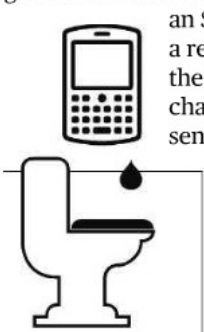


Group. The renamed Asurion acquired its main competitor, Lock/line, in 2006 and consolidated its position as the dominant cell phone insurer in the U.S.

Nearly 50% of claims are for lost or stolen phones

The carriers appear to benefit from wireless insurance, too. Asurion pays them billing fees for each policy they sell, which primarily covers administrative costs. Though he declines to get specific, Taweel also says that some carriers set up so-called captives, or insurance subsidiaries that allow the carriers themselves to finance the policies and reap some tax advantages. He argues, however, that Asurion's primary value to the carriers is reducing their customer "churn" or defections to rivals. Says Mark Siegel, spokesman at **AT&T Wireless**: "Cell phone insurance could give some customers additional peace of mind in the event they lose or damage their device. We benefit to the degree that it can help provide an additional measure of customer loyalty."

Consumer advocates point to Asurion's escalating revenue and profit as evidence the service is a bad deal for consumers. In certain cases, simple math bears them out. If a customer decides to get Total Equipment Coverage for a Verizon BlackBerry Curve 2, for example, an $8 charge shows up on the wireless bill each month. If the phone gets stolen or breaks, Asurion charges an $89 deductible to get a replacement. Here's the rub: There's a good chance Asurion will send that hapless BlackBerry owner a refurbished Curve 2, not a new one. Used Curve 2s currently sell for under $100 on eBay. For anyone more than one month into their phone contract, it may be a bad deal.



Top reason for damage claims: Phone dropped in toilet or other liquid exposure

Those refurbished phones may not even work that well. Robert Nissenbaum, owner of Blue Ridge Wireless Cell Phone Repair Center in Tucson, Ariz., sees many used phones from Asurion and other, smaller insurers: Customers bring them in, complaining of problems. "You tend to get phones back that aren't necessarily up to standard," he says. "We see a lot of people who say, 'This phone's really bad, I went through four of them,'" sending them in, over and over. He says cell phone insurers don't always use original manufacturer parts to fix phones, which can cause problems. (An Asurion spokesman says on the rare occasion that a part is not available from the original manufacturer, it finds other reputable suppliers.)

Taweel aggressively counters these complaints. He says only about half of all the phones Asurion sends out are refurbished, which is necessary when handset makers stop making a certain model or when there is limited supply of a hot new handset. He also says the company's customer satisfaction scores, as measured by an outside firm, are consistently high. Finally, he notes that Asurion offers not just financial protection but a sense of reassurance that the math doesn't capture. "If you are a cell phone insurance customer, you have until 10:00 p.m. central time to go onto our Web site, file a claim, and you are going to get that phone the next day," he says. "The alternative is to be without that service for some period of time, and then go in a store and get it replaced out of pocket. There's a huge hassle factor associated with it."



Cracked screens: 15% of claims. Common culprit: Sitting on device

Asurion has tried and failed to stay out of the limelight before. In 2008, Maryland Attorney General Douglas F. Gansler, whose wife was angered by the process of getting a replacement when their teenage son lost his cell phone, investigated whether the company was adequately disclosing all the caveats of its service such as the deductibles and used phones. Asurion maintained that it had not broken the law; after a six-month investigation, it agreed to pay a $1.5 million fine and enhance the clarity of its brochures. Gansler still does not believe the company is transparent enough. He'd like to see Asurion put the details of its policies on wall placards in cell phone stores—like the signs in rental car offices that disclose fuel costs. He also believes there is still a possibility that other AGs could bring similar actions against Asurion. "They are making billions a year by not telling people what they are buying," Gansler says. "If most people knew the actual terms, they wouldn't get it." *—Brad Stone and Olga Kharif*



10% of claims are devices run over by a car or otherwise entirely crushed

The bottom line *Asurion is the quiet provider of cell phone insurance for the top U.S. carriers. Consumer advocates say the policies are a bad deal.*

Social Networks

Now You Can Auction Off Your Coffee Run

▶ TaskRabbit connects people with "runners" who bid to do odd jobs

▶ It helps both parties "optimize their time and money"

We were too busy to write an article about TaskRabbit, so we posted a task—"write a freelance tech article"—on the site. The winning offer came from Laura Edgar, an out-of-work copy editor in El Cerrito, Calif., who says she finds jobs on TaskRabbit "about twice a month." —The Editors



Leah Busque and her husband Kevin were headed out for dinner in Boston one night in early 2008 when they realized they'd run out of food for their 100-pound Labrador, Kobe. Kevin mused that it would be nice if the couple could use the Web to find someone else to do the errand for them. Busque, a programmer for IBM at the

TOP, FROM LEFT: I LOVE IMAGES/ALAMY; PHOTOGRAPH BY DANIELLE LEVITT FOR BLOOMBERG BUSINESSWEEK

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time, decided that was a great idea. She registered the domain name RunMyErrand.com from her smartphone before they got to the first course.

Nearly three years later, RunMyErrand.com has gone from idea to startup. Now known as **TaskRabbit**, Busque's site is a network of several hundred "runners" willing to do short-term jobs on short notice. People who need the jobs done—"senders," as they're known on the site—post errands and the maximum amount they're willing to pay to have them completed. Runners then bid on the task. The sender can choose among them, or have the site do it based on factors that include price, speed, and the runner's reputation. TaskRabbit earns a small fee on each transaction.

Grocery shopping and assembling Ikea furniture are two of the most common requests, says Busque. The idea is to "allow people to live more efficiently, enjoy a better work-life balance, and optimize their time and money," she says.

Busque launched an early, Boston-only version of the site in 2008. She raised $2 million in venture capital in late 2009 and in June of this year expanded the service to San Francisco, where the eight-person company is now headquartered. She plans to expand to other cities soon and is also working on developing partnerships with corporations that want to make TaskRabbit available as an employee perk. **Google** recently completed a four-week trial in which employees in the San Francisco and Cambridge (Mass.) offices received TaskRabbit credits. (The search giant says it currently has no plans to extend the program.)

Busque acknowledges that not everyone is comfortable with contracting with strangers for work. TaskRabbit interviews potential runners over the phone and performs background checks before adding them to the network. The site also has a reviews section where runners and senders rate each other. Roberta Ponder of Danville, Calif., says she quickly grew comfortable with the site. She recently used a TaskRabbit runner to take a donation to the local library and says she was happy to find someone "to take care of it for such a small cost." —*Laura Edgar*

The bottom line *TaskRabbit is a site where busy people—including magazine editors—can find "runners" to do their errands for a fee.*



Kiva robots in Quidsi's New Jersey warehouse

Logistics

Rise of the Orange Machines

▶ E-commerce star Quidsi uses Kiva Systems' robots to cut costs

▶ "Now you can get Amazon in a bottle"

A decade ago, Mick Mountz was the logistics guy at dot-com-era e-grocery **Webvan**. He helped outfit warehouses with high-tech, 4.5 mile-long mazes of conveyor belts and carousels meant to sort, box, and deliver goods. The efficiency would be awesome; Webvan would make billions in the low-margin grocery business. That didn't happen. After Mountz quit in 2000 and the startup went bust the following year, he realized what was missing from his vision of automated warehouses: robots. He founded **Kiva Systems** in 2003.

The idea worked. Kiva robots are the backbone of **Quidsi**, the five-year-old owner of Diapers.com—and subject of *Bloomberg Businessweek*'s Oct. 11 cover story—that **Amazon.com** bought this month for $540 million. Kiva technology is also used by Amazon-owned shoe seller **Zappos.com**, **Gap**, and about a dozen other retailers, says Mountz.

The robots are squat contraptions that resemble fast-moving orange tortoises. They scurry around warehouses and bring shelves of clothing, electronics, car parts—whatever a retailer sells—to specialized workspaces called packing stations. There, humans pick out products, pack them into boxes, and push them onto trucks. The systems usually run in the $4 million-$6 million range. The cheapest, for $1 million, comes with 30 robots and two packing stations. All versions work with the customer's existing inventory-management software. Next year privately held Kiva will introduce a leasing program so companies can use its robots just during peak seasons. Mountz claims distribution centers that use his product can increase worker efficiency by up to four times.

He adds that Kiva doesn't just help customers handle more product; in some ways the technology actually becomes smarter than humans. In Kiva-run warehouses the robots continuously reorganize inventory based on order flow. For example, if there's an uptick in sales of corduroy pants, the robots place those items closer to the workers. Less popular merchandise gets relocated deeper into the facility.

An old rival for Lloyds' new CEO page 52 ▶



Quidsi co-founders Marc Lore and Vinit Bharara credit Kiva with helping them reduce costs enough to offer free overnight shipping to customers in about 70 percent of the U.S. (sorry, Hawaii and Alaska) on orders over $25. "Free shipping is now becoming the standard," says Cathy Halligan, a former executive at **Wal-Mart** who's now a senior vice-president at **Power-Reviews**, a service for adding customer reviews to websites. "If you can't run an operation at the lowest cost, you're going to bleed your P&L."

Lore and Bharara say the importance of logistics in Web commerce can't be overstated. They saw their opening after realizing most e-tailers focus on driving people to the website, not on back-end operations. Quidsi became so good at distribution that even Amazon, known for its logistical prowess, bought the company rather than compete with it, says Colin Gillis, an analyst at BGC Partners. (Amazon declined to comment.) "To succeed in e-commerce you have to control the supply chain," Lore says. "The bigger you get, the easier that gets."

Mountz certainly wouldn't dispute that. His pitch: Kiva's bots let the little guys get in the game. "Now you can get Amazon in a bottle," he says. "Everyone can have what Amazon has."

—*Joseph Galante*

The bottom line *Kiva Systems' warehouse robots help e-commerce stars cut costs and compete in low-margin businesses.*

Search Engines

How to Beat Google? Ask.com Can't Answer

▶ Barry Diller's search engine gives up—and will become a Q&A site

▶ "Google is getting to the point of absolute dictatorship"

Even larger-than-life media moguls can be cut down to size by **Google**. Barry Diller, 68, has run **Paramount Pictures** and **ABC Entertainment**, built **Fox Broadcasting** and the **USA Network**, and gamely battled fellow titans including John Malone and Sumner Redstone. Now he's waving the white flag of surrender in the direction of Mountain View, Calif.

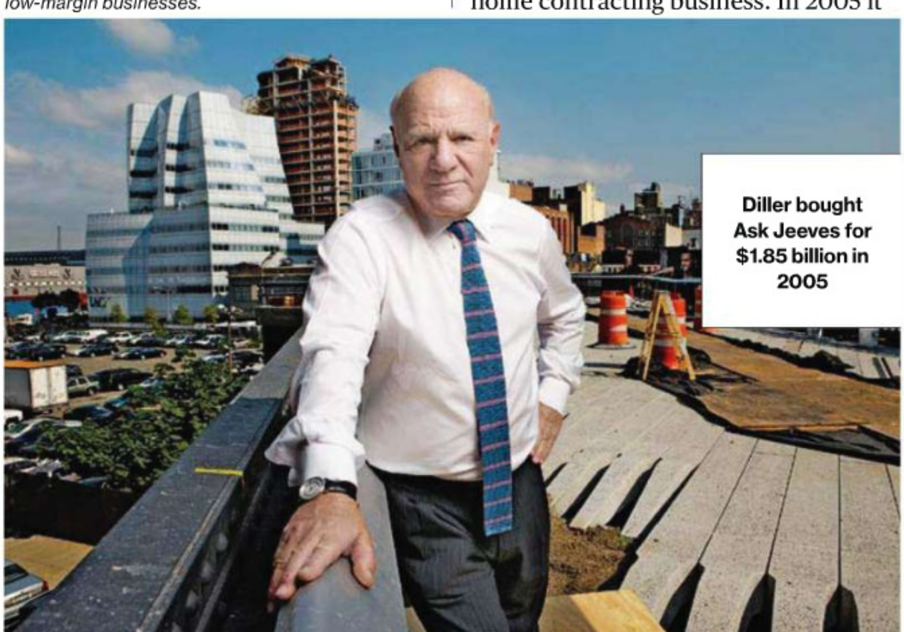
As first reported by Bloomberg News on Nov. 9, **Ask.com**, the Internet search engine that Diller acquired for $1.85 billion, is cutting 130 engineering jobs in New Jersey and China and refashioning itself as a question-and-answer site. In effect it's conceding the search business to the competition. "We've realized in the last few years you can't compete head-on with Google," says Diller.

Diller's New York-based **IAC/InterActiveCorp** controls multiple Web operations, including the **Match.com** dating site and the **ServiceMagic** home contracting business. In 2005 it added the search engine then known as Ask Jeeves to its portfolio. At the time, Ask Jeeves pitched itself as the place where regular people could pose questions in natural language and receive relevant search results. Diller renamed the site Ask.com in 2006 and pushed it to seek a stronger niche. Ask.com first tried to become a search engine focused on privacy by offering anonymous searches and then as a portal designed to appeal to women.

Diller found that it did not matter if he asked Jeeves, asked women, or just asked–nothing could stop the Google "juggernaut," as Ask.com President Doug Leeds puts it. Google is the No. 1 search provider in the U.S. and controls 65 percent of all searches, according to Nielsen. Ask.com ranked sixth and controlled less than 2 percent of the market. In an interview last June, Diller noted that "Google is getting to the point of absolute dictatorship." In February, IAC took a $991 million impairment charge for its search and media business, which includes Ask.com.

The site will still feature a prominent search box on its homepage, but the results will be delivered by one of its former competitors. Leeds declined to specify which company got the business, citing a confidentiality agreement. Despite the anti-Google rhetoric, IAC has had a partnership with the search giant since 2008. Under the arrangement, Ask.com used Google search results for some queries, and the two companies shared ad revenues. The deal runs through 2012. **Yahoo!**, another beleaguered Internet giant, has also ceded its search business to competitors. In 2009 the Sunnyvale (Calif.) company signed a 10-year agreement to use **Microsoft** Bing search technology on its Web properties.

Diller isn't surrendering entirely. Ask.com will consolidate its engineering operations at headquarters in Oakland, Calif., and focus on developing its Q&A service. The feature aims to provide definitive answers to questions rather than a string of search results. Someone who types in the query like "What's the weather in Cleveland?" will receive a direct answer at the top of the page rather than having to click through to a weather-related site. Answers will be culled from relevant Web sites or, where appropriate, from hand-



Diller bought Ask Jeeves for $1.85 billion in 2005

CLOCKWISE FROM TOP RIGHT: PHOTOGRAPH BY JONATHAN ROBERT WILLIS FOR BLOOMBERG BUSINESSWEEK; BEN BAKER/REDUX; DOMINIC LIPINSKI/PA/AP PHOTO

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crafted responses by members of the Ask.com community.

Ask.com may be sidestepping Google, but it will face competition from Q&A-focused Silicon Valley startups such as **Quora**, **Formspring**, and **ChaCha**. Aardvark, a similar site, was bought by Google earlier this year. **Facebook** recently began its own Q&A feature as well.

Ask.com believes it has advantages over these other sites, in particular its large audience: The site still receives 90 million unique visitors a month, according to ComScore. "People already know us for questions and answers," says Leeds, who says that 40 percent of the search queries on its page are already posted in the form of questions.

The new Ask.com will have to develop a community of well-informed contributors to answer questions posed by users. The site recently sent surveys to some of its members to assess their areas of expertise and interests. Ask.com will soon begin using Facebook and **LinkedIn** to supplement the data it already has. Leeds says Ask.com's engineers are working on ways to quickly match questions to the appropriate experts. The company hopes to make money in part by allowing advertisers to pay to answer certain questions.

Despite the turmoil at Ask.com, IAC's search division is still growing: Third-quarter revenues increased 20 percent from the previous year, to $205.1 million, and operating income rose 43 percent, to $28.9 million. The success is largely thanks to the division's toolbar business, says Sandy Mehta, an analyst at Hong Kong-based Value Investment Principals. Toolbars are add-ons to Web browsers, websites, and software products, and give users quick access to search functions (which will now be powered by Ask.com's unnamed partner). IAC provides few details on how it earns money through the toolbar, but Mehta says the business is "really growing. ... It's sort of a backdoor surge."

Mehta is not nearly so sanguine about the latest changes at Ask.com. "Q&A is really not much different than Ask.com currently," he says. "Gradually, Ask.com is sort of fading away."

—Brad Stone and Brett Pulley

The bottom line *IAC/InterActiveCorp is outsourcing its search technology and reorienting Ask.com as a Q&A site. Its toolbar business is still growing fast.*

Innovator

Marc L. Ingram



As a high schooler, Ingram built a device to let his dad start his car's heater from a cell phone. Now the 24-year-old wants to go up against OnStar

By 2002, Marc L. Ingram had grown tired of hearing his dad complain about his long, cold walk through the parking lot after work at the General Electric facility in Louisville. Ingram, a high school freshman at the time, remembers his father often saying he wished he could start his car remotely "so that by the time I get there it'd be all warmed up." The 15-year-old decided to get out his toolkit.

Within a few months the Wireless Auto-Attendant was born. Ingram used his coding skills to program a small cellular receiver. He plugged the receiver into the diagnostic port underneath the dashboard of his dad's car. (It's the slot where mechanics connect equipment to the onboard computer.) The receiver relayed commands from a mobile phone to the car, so that by dialing a few numbers Ingram's dad could start the engine, lock or unlock the doors, and turn on the heat or air-conditioning from anywhere. During Ingram's senior year of high school in 2005, the device took fourth place in the engineering category of the Intel International Science and Engineering Fair.

Ingram, now 24 and two years out of college, has been tinkering with it ever since. In late 2009 he entered into a partnership with **Samtec**, a maker of electronics components in New Albany, Ind. The company agreed to fund a new venture, **Mavizon Technologies**, to produce and market the gadget, now known as AutoBot. Like the prototype, AutoBot connects any car built after 1995 to cellular networks and lets a user control all the same functions. It also checks oil levels and other diagnostics, can disable the car remotely if it's stolen, and can detect a crash and automatically send an emergency message to friends and family. The AutoBot functions can be controlled from a smartphone app or a Web browser.

Mavizon will start selling the lipstick-tube-size AutoBot for $299 in early summer. Users must also pay a monthly service fee that is yet to be determined, though Ingram hopes to offer an advertising-supported version without the recurring charge. Ingram will have plenty of competition: Companies such as **Directed Electronics** and **DevToaster** are working on similar products. All of them will compete with existing products such as **General Motors**' OnStar, which starts at $19 a month and comes standard on GM vehicles. The new entrants deliver "the same functionality by letting you install a piece of software on your phone," says Dominique Bonte, director of telematics and navigation for ABI Research.

Ingram says AutoBot will stand out from the crowd by innovating. Future products from Mavizon will stream music and news from the Web to a car's audio system, for example. "My vision has grown out of a lot of small ideas," he says. *—Cliff Edwards*

Inspiration ▶ **His dad's cold walk through a parking lot to his car**

Recognition ▶ **Won fourth place at the Intel Science Fair**

Future ▶ **A $299 gadget that will compete with OnStar**



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Until Amelia Earhart became the first woman to fly solo across the Atlantic, she would not rest.
Nor would her technical advisors. (Newfoundland, 1932.)



Until my client *knows* that I put her first.

Until I understand what drives her.

Her goals. Her ambitions. Her commitments.

Until I know how to make those goals, ambitions and commitments my own.

Until she knows I understand what she's up against.

An economy on the back foot.

An investment world forever changed.

A set of priorities that have been realigned, not always by choice.

Until she sees how our tailored Wealth Management Research can help her recover some of her confidence.

And how my access to that research makes me more nimble, more agile, and better prepared for whatever the market does.

Until she knows that I'm always thinking about her investments.

Whether she is or not.

Until then...

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Modifications Aren't Stopping Foreclosures

▶ **Borrowers are being evicted while in programs meant to keep them in their homes**

▶ **"It's more common to hear that banks have lost paperwork than ... properly handled it"**



Gray moved to a rental in Mesquite, Tex., after she lost her home

PHOTOGRAPH BY MISTY KEASLER FOR BLOOMBERG BUSINESSWEEK

Jill Gray of Mesquite, Tex., says her three-year-old son, Anthony, often tells her before he goes to bed: "I wanna go to the other house." Last month Gray, Anthony, and Tiffy, their black Labrador mix, moved about 12 miles to a rental after their one-story brick house in Garland was auctioned in a foreclosure. Gray, 38, tried for almost a year to get her mortgage modified. **Bank of America** initially agreed, only to rescind approval, telling Gray that documents were missing—documents that Gray says she sent.

Gray's experience of being evicted while participating in a program designed to avert foreclosures is being repeated thousands of times at the biggest mortgage firms, according to groups that aid borrowers. The government's Home Affordable Modification Program (HAMP) came under fire at hearings late last month for granting homeowners "trial modifications" during which late fees and debts can stack up and documents can disappear, triggering foreclosures.

"Many homeowners end up facing foreclosure solely on the basis of the arrears accumulated during a trial modification," said Julia Gordon, senior policy counsel at the Center for Responsible Lending, in congressional testimony on Oct. 27. "One incomplete payment or one accounting mistake can land you on an apparently unstoppable conveyor belt to eviction."

With as many as 7 million homes facing foreclosure or already taken, according to real estate website Zillow, both the government and companies such as Bank of America and **JPMorgan Chase**, the two biggest U.S. lenders, offered programs to forestall seizures by easing mortgage terms. Changes include cutting interest rates for as long as five years and extending repayment to 40 years. About half the 1.4 million temporary or trial modifications granted since the program's March 2009 inception have been canceled, according to Treasury Dept. data. Only 466,708 borrowers have received permanent modifications. About one in five of the canceled modifications is either in foreclosure or bankruptcy, according to a Treasury survey of the nation's eight-largest mortgage servicers, which handle billing, collections, and foreclosures.

Even borrowers who do win approval and never miss a payment can wind up in foreclosure, the Office of the Special Inspector General for the Troubled Asset Relief Program said in an Oct. 26 report to Congress. "They may face back payments, penalties, and even late fees that suddenly become due on their 'modified' mortgages and that they are unable to pay, thus resulting in the very loss of their homes that HAMP is meant to prevent," according to the report.

Mortgage firms make the problem worse by losing paperwork, according to testimony from Richard H. Neiman, the New York State superintendent of banks. In a May and June survey of 40 counselors representing as many as 14,000 borrowers, the California Reinvestment Coalition found that all of them said servicers had lost or ignored docu-



Gray's former home in Garland, Tex., is on the market for $55,000.

ments, according to Associate Director Kevin Stein, whose San Francisco organization works with low-income communities. "It's more common to hear that banks have lost paperwork than to hear that they received it and properly handled it," says Joseph Ridout, a spokesman for Consumer Action, a San Francisco education and advocacy group with a network of 9,000 community organizations nationwide. That leaves HAMP participants vulnerable to foreclosure, a process that has been tainted by allegations of "robo-signing," in which mortgage firms sign and submit court documents to justify home seizures without verifying they were accurate. Attorneys general in all 50 states are investigating.

Under HAMP, homeowners have their mortgage payments reduced to 31 percent of their monthly gross income. The process often results in them owing more money because accrued interest and other charges are tacked onto the mortgage balance. Some HAMP modifications add so-called balloon payments to the loan that are due when a house is sold or the loan paid off. "The program continues to perform well," says Andrea Risotto, a Treasury spokeswoman. "The target of affordability that HAMP put in place—this idea of 31 percent debt to income, which was far more aggressive than what was done historically—is helping homeowners sustain the modification."

Spokesman Tom Kelly says JPMorgan is able to track paperwork because it scans every document as soon as it's received. At **Ally Financial**, spokeswoman Gina Proia says the lender requires homeowners to submit paperwork at the start of the modification process, leading to a "higher likelihood" of permanent modifications and lower re-default rates. Jumana Bauwens, a Bank of America spokeswoman, declined to comment on matters tied to lost paperwork.

Gray, the former homeowner in Texas, says she fell behind on her mortgage bills last year after paying for medical treatments for her son that weren't covered by insurance. She says she received the modification offer from Bank of America in December and immediately signed and returned the contract, using the supplied FedEx envelope. Bauwens said the bank didn't receive it by the due date. Gray kept a record of her calls to the bank and printed confirmations of documents she faxed. The log reads, in part: "Sept. 9: Called, was disconnected. Called again. Spoke to Christina. While transferred to supervisor I was disconnected." When her home was auctioned in September, there were no bidders, so it reverted to the mortgage holder, **Freddie Mac**, which was taken over by the government in 2008. The house is now listed for sale at $55,000.

Gray is again being considered for a modification, and the foreclosure sale may be rescinded, Bank of America's Bauwens says. Gray, who works in the building-permit department in a city called Fate and is a part-time Avon Products saleswoman, says she doesn't expect to be approved. She's paying $775 a month in rent, boosting her monthly outlays beyond the program's guidelines on income and expenses.

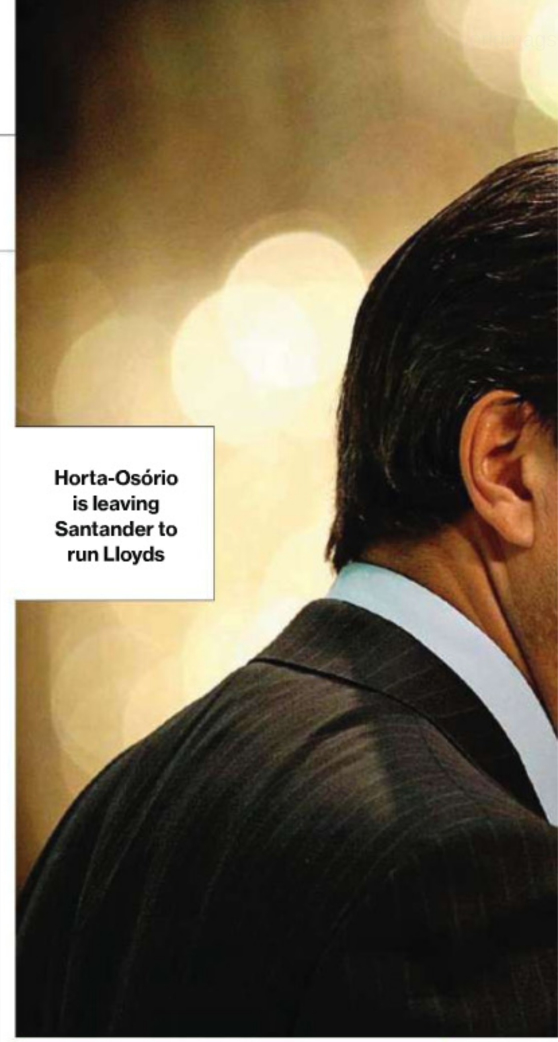
—*Kathleen M. Howley, Dakin Campbell, and Danielle Kucera*

The bottom line *Programs meant to prevent foreclosures don't work for many homeowners who participate, in part because of paperwork errors.*

25

MILLION DOLLARS

The amount Goldman Sachs will lend to a nonprofit community development group to finance 16 charter schools in New York City and New Jersey



Horta-Osório is leaving Santander to run Lloyds

European Banks

Lloyds' New Chief Faces a Familiar Rival

- Horta-Osório will compete against Santander's heir apparent
- "He goes into it with his eyes wide open," says Chairman Bischoff

After 18 years working for Chairman Emilio Botín at Spain's **Banco Santander,** António Horta-Osório may have tired of waiting for the chief executive officer's job. Horta-Osório, 46, is becoming CEO of **Lloyds Banking Group**, taking a "substantial" pay cut, Lloyds Chairman Winfried Bischoff said when he announced the appointment on Nov. 3. The same day, Santander said that Ana Patricia Botín, Emilio's 50-year-old daughter, will replace Horta-Osório atop the bank's U.K. unit.

Horta-Osório, who brings with him secrets picked up over four years running Santander in the U.K., will be competing head-to-head with his former company and the family that built it. The family's longstanding grip on the company—three Botíns have served as chairman—may have contributed

HORTA-OSORIO: DOMINIC LIPINSKI/PA/AP PHOTO; BOTIN: DOMINIQUE FAGET/AFP/GETTY IMAGES

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to his departure. "Possibly he felt he was being pushed toward the exit door to make way for Ana Patricia Botín," says Andrew Lim, a financial analyst at Matrix Corporate Capital in London.

While Santander, Spain's biggest bank, has been expanding, Lloyds, based in London, has been shrinking since a U.K. taxpayer-funded rescue in 2008. Under Horta-Osório, Lloyds will need to pay down the almost £120 billion ($193 billion) it still owes the central bank and the British government and earn a return on the state's equity stake for taxpayers. He also will have to give evidence to a government commission on banking competition next September, arguing against a breakup of the bank, which controls about a quarter of U.K. mortgage lending and is now 41 percent state-owned. Horta-Osório, who will take over on Mar. 1, replacing J. Eric Daniels, is aware of the challenges.

"He goes into it with his eyes wide open," Bischoff said.

Lloyds "has to be taken to the next phase of its development," Horta-Osório said on a conference call in London with reporters on the day of the announcement. "This is probably the only bank in Europe for which I'd consider leaving Santander." He declined to comment for this story.



Ana Patricia Botín

Horta-Osório built Santander's U.K. unit into the country's second-biggest mortgage lender after becoming CEO in 2006, in part by helping acquire mortgage bank **Alliance & Leicester** and units of **Bradford & Bingley.** Since 2008 profits have climbed 68 percent at the unit, which accounted for 18 percent of Santander's overall earnings in the third quarter. Santander said on Oct. 28 that it planned to sell a stake in the U.K. business in an initial public offering that would probably take place in the first part of 2011.

Before being named to her new post, Ana Patricia Botín had led Santander's Spanish retail unit Banesto. On her watch, Banesto survived Spain's real estate collapse without posting a single quarterly loss. After earning an economics degree at Pennsylvania's Bryn Mawr College in 1981 and working for J.P. Morgan in Madrid and New York, she took her first job at Santander in 1988. "Her path has been very carefully prepared," says Robert Tornabell, a professor of finance at the ESADE business school in Barcelona. Her new post "would be the last step" on the road to succession, he says.

Horta-Osório, who speaks four languages, earned his MBA from INSEAD in 1991 and was hired by Emilio Botín from **Goldman Sachs** in 1993 to run Santander's Portuguese investment banking unit. He says his move to Lloyds was influenced by his growing attachment to Britain, where he lives with his wife and three children.

The Portuguese national, a master scuba diver who has gone cage diving with sharks, says he saw the job of rebooting the bank as a way of helping put the U.K. economy back on its feet. "The success of Lloyds is inextricably linked to the success of the British economy," Horta-Osório said on the conference call. "I really like your country, the culture of tolerance. This is the country where my wife and I decided we want to see our children grow up." *—Ben Sills, Jon Menon, Emma Ross-Thomas, and Charles Penty*

The bottom line *Moving from Santander to Lloyds, Horta-Osório will be competing against the daughter of his former boss.*

Finance

A Wall Street Product That Soaks Taxpayers

▶ **Sold as a way to save money, swaps ended up hiking costs**

▶ **"No reason these entities should be playing with this stuff"**

The subprime mortgage crisis isn't the only Wall Street-created calamity upending the finances of U.S. states and cities. For more than a decade, banks and insurance companies convinced governments and nonprofits that using swaps contracts would lower interest rates on bonds sold for public projects such as roads, bridges, and schools.

It didn't work out that way. Since the credit crisis began in 2008, failed swaps deals have cost more than $4 billion as hundreds of borrowers, from the **Bay Area Toll Authority** in California to Harvard University, quietly pay Wall Street firms to end interest-rate swap agreements. The termination payments to Wall Street firms come at the worst possible time. States will face budget gaps of $72 billion next fiscal year, according to the National Conference of State Legislatures.

Borrowers terminate swaps—the cost is determined by current interest rates and other factors—because doing so may be cheaper than continuing to make payments. The California Water Resources Dept. this year spent $305 million unwinding interest-rate bets that backfired, paying banks led by New York-based **Morgan Stanley**. North Carolina paid $59.8 million in August, enough to cover the annual salaries of 1,400 full-time workers. Reading, Pa., got caught on the wrong end of a deal, costing it $21 million, equal to more than a year's worth of real estate taxes. "It was brilliant, and it all blew up on me," says Brian Mayhew, chief financial officer of the Bay Area Toll Authority. In July 2009 the state agency paid $105 million to **Ambac Financial Group**, the bond insurer that filed for bankruptcy on Nov. 9, to dissolve $1.1 billion of interest-rate agreements.

In all, borrowers have made more than $4 billion of termination payments to companies including **Citi-**



The best B-schools of 2010 page 77 ▶

group, **JPMorgan Chase**, and **Bank of America** since the beginning of 2008, according to a review of hundreds of bond documents and credit-rating reports by Bloomberg. Alexander Samuelson, a Citigroup spokesman, declined to comment, as did Mary Claire Delaney of Morgan Stanley, Justin Perras of JPMorgan Chase, and Danielle Robinson of Bank of America. In September 2008, JPMorgan said it would stop selling interest-rate swaps to government borrowers.

Few taxpayers are aware of the cost of untangling municipal swaps. The only disclosure of the payments to Wall Street often is buried in documents the borrowers have to give investors when they sell bonds. In many cases, the firms getting the payments aren't explicitly identified, and government officials often don't call attention to the payments made to cancel contracts. Many telephone calls and e-mails from Bloomberg News to dozens of government and nonprofit officials over the last eight months seeking comment on derivatives transactions went unanswered.

Wall Street banks and insurers peddled $500 billion of interest-rate swaps to governments and nonprofits before the credit crisis, says a report published by the International Monetary Fund in June. In a typical transaction, a borrower would sell bonds with a variable interest rate. At the same time, it would enter into a swap that required it to pay a fixed interest rate to a bank or insurance company, which would pay the borrower a variable rate. The net result was that the bond issuer paid a lower interest rate than it would have if it had simply issued conventional fixed-rate bonds. That's how it was supposed to work. When interest rates plunged during the credit crisis, the banks and insurance companies started paying much less to the governments and nonprofits on the other end of the swaps, turning the deals into money losers for the borrowers.

While banks got paid to underwrite municipal bonds for public projects, they were able to generate additional fees if the borrower used a swap with the transactions. Because the contracts were unregulated and privately negotiated, the profits that Wall Street booked were not disclosed. "The basic idea from the bank's perspective is just to do a swap because that's where the money is," says Andrew Kalotay, head of the debt management advisory firm Andrew Kalotay Associates in New York. "Look at all the fees they get."

In addition to getting termination payments, Wall Street is finding another way to profit—underwriting bonds that borrowers are selling to raise money for the termination fees and to refinance their variable rate debt. Morgan Stanley, JPMorgan Chase, and Bank of America were among the firms that got termination payments from California's Water Resources Dept. this year at the same time they were paid to help the state agency sell its bonds, according to offering documents.

"There's just no reason these entities should be playing with this stuff," says Christopher Whalen, managing director at Torrance (Calif.)-based research firm Institutional Risk Analytics. "They don't have the capacity to evaluate these instruments. They are totally lost."
—Michael McDonald

The bottom line *Borrowers are paying billions of dollars to get out of swaps deals, which backfired when interest rates plunged.*

Paying for Bad Bets

The 10 highest fees paid by government and nonprofit borrowers to terminate swaps contracts, according to a Bloomberg survey

Borrower	Fee (Million)
Harvard University	$497.6
California Water Resources Dept.	$305.4
Bay Area Toll Authority, Calif.	$105.0
Vanderbilt University	$87.2
Miami-Dade Water and Sewer Dept.	$76.4
North Carolina	$59.8
Penn. Intergovernmental Cooperation Authority	$52.8
Pennsylvania Turnpike Commission	$52.7
Rensselaer Polytechnic Institute	$50.0
New York State Urban Development Corp.	$47.6

Auto Stocks

Sizing Up GM as It Gets Ready for Its IPO

▶ The company could earn $19 billion a year if the car market booms

▶ "The question is whether they can execute the product portfolio"

In advance of **General Motors**' Nov. 17 initial public offering, Chief Executive Officer Daniel F. Akerson, Chief Financial Officer Christopher P. Liddell, and four other executives have been on the road chatting up investors—and making some ambitious projections.

GM says it could reach operating profits of up to $19 billion if the U.S. market returns to near-record annual sales levels of 17 million vehicles, according to two people familiar with the company's presentation. In a midlevel market of about 15 million vehicles, the automaker could generate as much as $13 billion in earnings before interest and taxes, Liddell said in a meeting with investors in New

FROM TOP: ROBYN BECK/AFP/GETTY IMAGES; ILLUSTRATION BY DARKOW/COLUMBIA DAILY TRIBUNE/CAGLE CARTOONS

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GM has big hopes for its Chevy Cruze compact

York on Nov. 8, according to the people, who asked not to be identified because the meeting was private.

The record for U.S. light-vehicle sales was 17.4 million in 2000. Sales last year fell to 10.4 million, according to researcher Autodata. Liddell didn't say when he expects to see auto sales climb to 15 million or higher. GM uses Lexington (Mass.)-based research firm **IHS Automotive** for forecasting. IHS predicts that auto sales will reach 15 million vehicles in the U.S. in 2012 and 17 million in 2015.

In a video on the website RetailRoadshow.com, Liddell says that to break even, GM previously needed 25 percent of a U.S. market of 15.5 million vehicles a year. It can now be profitable with about an 18 percent share of a 10.5 million market. The new GM is "fundamentally different than the old GM," he says.

It's hard to argue with that. The company's U.S. labor costs are $5 billion, one-third what they were in 2005. Bankruptcy in June 2009 allowed it to close factories and shed weaker brands. The automaker, 61 percent-owned by the U.S. government, reported net income of $2.16 billion for the third quarter; it has made $4.8 billion this year.

GM has big hopes for the Chevrolet Cruze, a compact that went on sale in September and will soon come in a version that boasts highway fuel economy near 40 miles per gallon. In 2011 it will unveil a new Chevy Malibu, and a small Cadillac is due around 2013 to battle **BMW**'s 3 Series. "I'll give it a hard look," says Brett D. Hoselton, senior auto analyst with KeyBanc Capital Markets in Cleveland. "The question is whether they can execute the product portfolio strategy three to five years from now."

GM hopes to sell $10.6 billion in stock, representing 24 percent of the equity in the company, at $26 to $29 a share in the IPO. A $29 price would give the company a market value of $44 billion. Morningstar analyst David Whiston estimates GM's stock would trade at 13.3 times this year's earnings per share, well above **Ford Motor**'s price-earnings ratio of 7.9. Whiston thinks the rich valuation is more than justified. "GM is going to print money once car sales come back," he says. —*David Welch*

The bottom line *While GM has made progress since its bankruptcy, its success depends on a stronger economy leading to a big increase in car sales.*

Drawing Board



Mutual Funds

Why Janus Overseas Is Betting on the U.S.

▸ With emerging markets pricey, manager Lynn looks homeward

▸ "There are interesting things going on under the surface"

Brent Lynn has beaten 96 percent of rivals since taking over the **Janus Overseas Fund** in 2003, in part by investing in stocks from emerging markets such as India and Brazil. Now Lynn is finding attractive bets closer to home. **Delta Air Lines**, **Ford Motor**, and **Bank of America** were among the top 10 holdings as of Sept. 30 at the $13 billion mutual fund. Over the past three years, Lynn has more than doubled his weighting in U.S. stocks, to 20 percent—the most the fund is allowed to hold—while cutting emerging-market holdings to 23 percent from 37 percent. "Some of the best investing opportunities may be in the developed markets of the U.S. and Europe," says Lynn from his office in Denver, where **Janus Capital Group** is based. "Growth may not be as exciting as it is in some emerging countries, but there are interesting things going on under the surface."

Lynn, 46, is one of a growing number of money managers who say the rush into emerging-market stocks has driven up their prices to the point where it's hard to find bargains. "The emerging-market story is as great as it has ever been, but the prices you are being asked to pay to participate are increasingly full," says Simon Hallett, chief investment officer at Harding Loevner in Somerville, N.J., which has $10 billion in assets under management, including $4 billion in equities of companies in developing countries.

The MSCI Emerging Markets Index gained 19 percent this year through Nov. 5, including dividends, compared with a 12 percent increase for the Standard & Poor's 500-stock index. Emerging-market stocks jumped 79 percent in 2009, triple the 26 percent return of the U.S. benchmark. Since Lynn became manager, Janus Overseas has returned about 19 percent a year, according to research firm Morningstar. This year it has gained 20 percent.

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Markets&Finance

In the fourth quarter of 2008 and the first quarter of 2009, Lynn pared the number of stocks in the portfolio and put money into companies with the financial strength to survive the crisis. Among them were Hong Kong-based exporter **Li & Fung**, the biggest supplier to **Wal-Mart Stores**, and Mumbai-based **Reliance Industries**, owner of the world's largest fuel-refining complex. The stocks, now Lynn's two biggest holdings, have been among the fund's top positions for the past four years, regulatory filings show. Li & Fung shares have more than tripled since their October 2008 low; Reliance has more than doubled.

While seeking stocks with strong growth potential, Lynn also looks for what he calls special situations—companies or industries undergoing structural changes that have yet to be recognized by other investors. To Lynn, airlines fit that definition. U.S. carriers have removed seating capacity in the past few years "at a rate we believe is unprecedented since World War II," he says. With fewer tickets available, they can charge higher prices and generate greater profits. The Bloomberg U.S. Airlines Index has climbed 36 percent this year. Lynn owned stakes in Atlanta-based Delta and Houston-based Continental Airlines as of June 30, Bloomberg data show. Continental merged with United Airlines on Oct. 1, creating **United Continental Holdings**.

19%

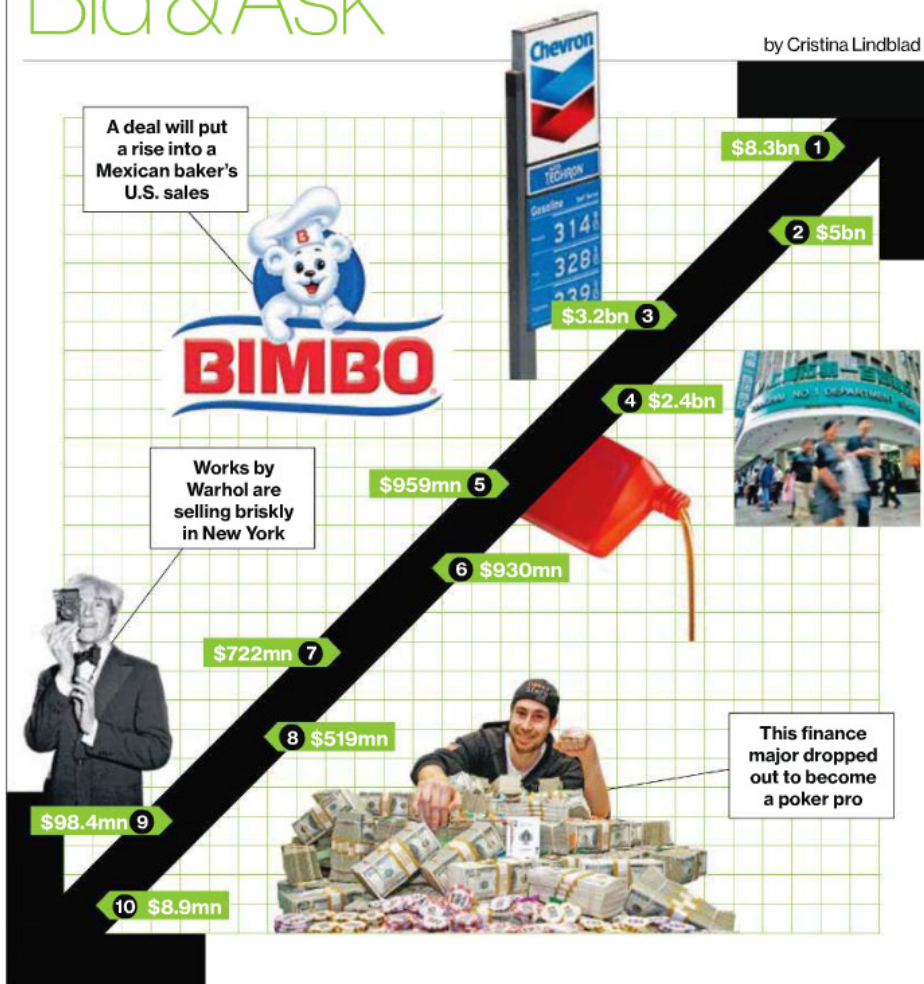
The gain in the MSCI Emerging Markets Index this year through Nov. 5

Shares of Ford, Lynn's fourth-largest holding, gained 62 percent in 2010 as it grabbed market share from weaker rivals and commanded higher prices. Ford has the potential to capture a larger piece of the small-car market, Lynn says. Bank of America, whose stock has fallen 18 percent this year, still faces economic and regulatory uncertainty, he says. Lynn is hanging on: "I believe those problems mask the company's long-term earnings power."
—*Charles Stein*

***The bottom line** Lynn's shifting money in the Janus Overseas Fund to the U.S. is another sign emerging markets may be overheating.*

Bid & Ask

by Cristina Lindblad



1 **BlackRock** stakeholders Bank of America and PNC Financial Services sold $8.3 billion of stock in the New York-based investment firm, the biggest stock offering in the U.S. this year.

2 **Vodafone Group** will sell its minority stake in Japanese mobile carrier SoftBank for $5 billion to focus on data services and other higher-growth areas.

3 **Chevron**, the No. 2 U.S. oil company, agreed to buy Atlas Energy for $3.2 billion, giving it access to the Marcellus Shale, an area in Pennsylvania rich in natural gas.

4 **Shanghai Friendship Group** is acquiring rival department-store chain Shanghai Bailian Group for $2.4 billion in a union brokered by Chinese authorities.

5 Mexico's **Grupo Bimbo** is buying Sara Lee's North American bakery business for $959 million. Bimbo already has several well-known U.S. brands in its basket, including Entenmann's cakes and Thomas' English Muffins.

6 **Ashland**, maker of Valvoline motor oil, sold its chemicals distribution unit to private equity firm TPG Capital for $930 million.

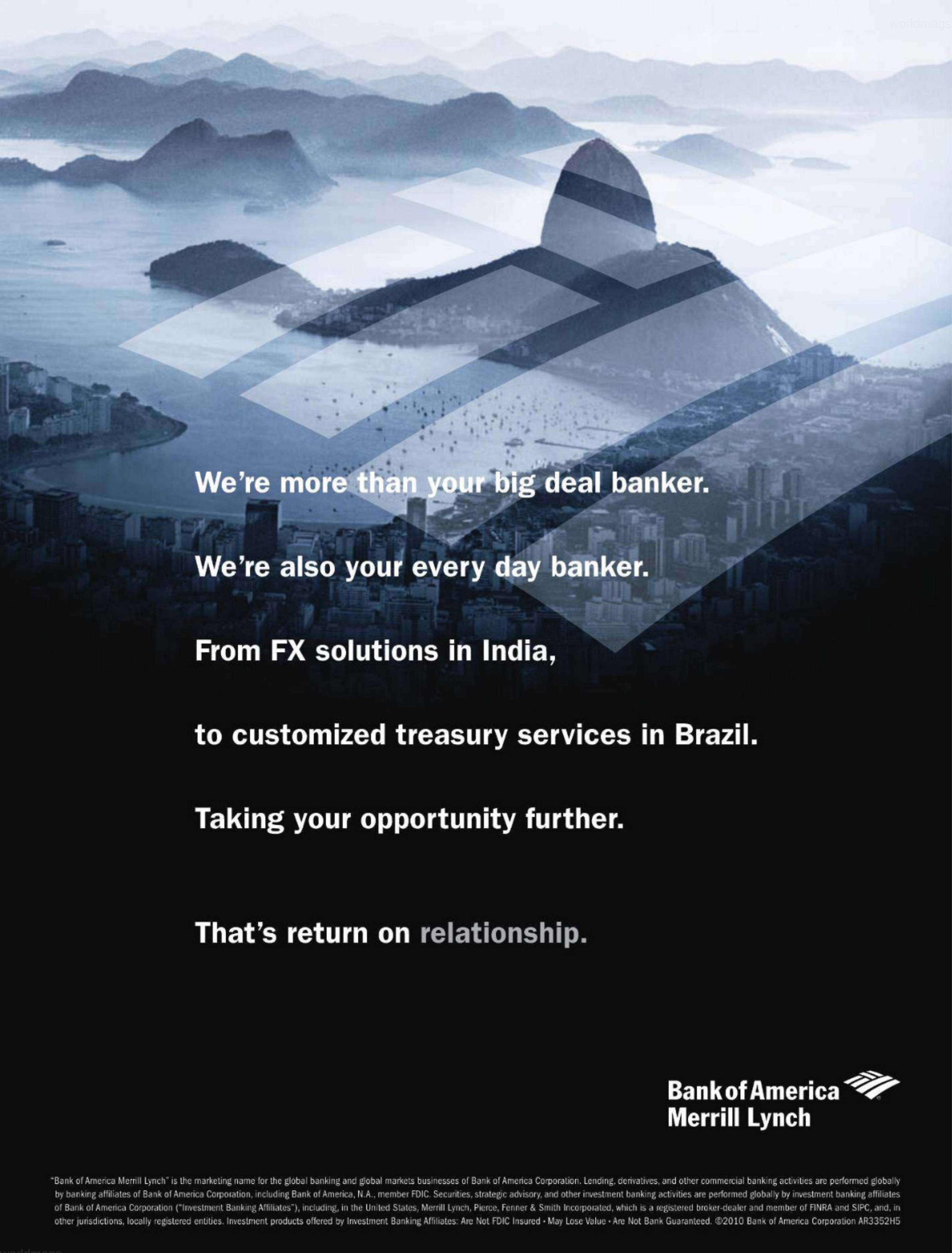
7 **Norway's sovereign wealth fund** is paying $722 million for a 25 percent stake in a portfolio of 113 buildings on Regent Street, one of London's busiest shopping areas.

8 **Strabag** received a $519 million investment from Russian billionaire Oleg Deripaska. The Austrian construction firm has been tapped to build some facilities for the 2014 Winter Olympic games in Sochi.

9 **Andy Warhol** was the star of the contemporary art auctions in New York, with a total of 19 works up for sale. Two standouts—a painting of a Coke bottle and a silk screen of Elizabeth Taylor—fetched a combined $98.4 million.

10 **Jonathan Duhamel**, a 23-year-old Canadian, won the $8.9 million first prize at the World Series of Poker.

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Charlie Rose talks to

Mary L. Schapiro



The chairman of the SEC on rolling out financial reform, reining in high-frequency trading, and ensuring the integrity of the markets

Everybody's waiting for the [financial reform] rules to be defined. How do you view that task?
I view it as enormously important that we get it right. We have to deliver a set of cogent, responsible rules that animate and implement the Dodd-Frank legislation. We have over a hundred rules to write, more than 20 studies to conduct. We have to create five new offices within the SEC. We're involved in over-the-counter derivatives, hedge fund regulation, credit-rating agencies, fiduciary duty, corporate disclosure requirements. We've got multidisciplinary task forces working on each set of rules. We're pushing out proposals at a pretty good clip, largely [for] those that are required to be implemented by July 2011.

Was the settlement with Goldman Sachs intended to send a message that this is a new sheriff in town?
No, it was intended to address what we saw as violations of the federal securities laws. It also hopefully informed the industry about conduct that we think is problematic.

What happened on May 6?
May 6 was a really unfortunate experience for our markets and for American investors. In the space of several minutes, the Dow declined 573 points, and then in even less than several minutes recovered by 543 points. We can't have a system here where people are uncomfortable about the integrity of the marketplace. We'll never take all the risk out of investing, nor should that ever be our goal. But if confidence in the integrity of the marketplace is even a small reason for investors to pull out, I think that's a terrible thing. We have to get to the bottom of fixing the fragmented and loose structure of our markets that contributed to that.

How are you going to do that?
We've done a number of things already that we think have made an enormous difference. Immediately after May 6, we brought in all the exchanges and quickly got agreement to put into place circuit breakers that require that if a stock moves more than 10 percent up or down in five minutes, trading in that stock is halted for five minutes while the primary listing market has the opportunity to gather liquidity and reopen the stock at a more rational price. We had some stocks execute at $100,000 a share on May 6; you don't hear as much about those as the ones that executed for a penny. The single-stock circuit breakers, which initially applied just to the S&P 500, now have been extended to the Russell 1000 and hundreds of ETFs and have made quite a big difference. They've been triggered about a dozen times, which has been an interesting laboratory for us.

The real problem was nobody knew going into the process, at what price would trades be broken? That caused some liquidity providers to not be in the market because they were afraid they would put on a trade that would be broken because there was no clarity around what levels of pricing would result in broken trades. That issue's been resolved with the new erroneous trade break rules. We also passed a final rule that says a broker-dealer can't allow a customer to directly access the marketplace without going through the broker-dealer's risk management controls. Had that rule been in place over the last six months, some erroneous trades would never have gotten into the marketplace.

But now we have a lot of other things on our plate that we need to do that are a direct response to May 6. So we're looking at broader market structure issues. Should market makers have obligations again to buy and sell in volatile markets? Should we have more robust regulation of high-frequency traders?

Where are you on that?
We're getting close. We put out a concept release back in January, and we asked hundreds of questions about what is the role of high-frequency trading in our markets? Is it a good role, is it a negative role? What's the role of algorithms? Should algorithms be required to be programmed with throttles to slow them down or change their conduct depending upon different activities happening in the marketplace? Should we have greater transparency about what activities are taking place in our markets?

All of these issues have been out for comment. We've gotten hundreds of thoughtful comment letters, and now we're in the process of laying out a road map for our commission to think about all the discrete actions that we could take—building on the ones we've already taken—that we hope will lead us to a more stable marketplace. Ⓑ

The interview was conducted at the annual meeting of the Securities Industry and Financial Markets Assn.



Watch Charlie Rose on Bloomberg TV weeknights at 8 p.m. and 10 p.m.



Next.

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How

Robin Li banged heads to beat Google and make his search engine No. 1 in China. His next target: The rest of the world



Won

Li gets prepped for his speech at the annual Baidu World conference in Beijing



Baidu China

By Brad Stone and Bruce Einhorn
Photographs By Andrew Rowat

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Many CEOs have admirers.

Robin Li–the 41-year-old, American-educated chief executive officer of the Chinese search engine Baidui–has a fan club.

And each year at the Baidu World conference in Beijing, the members of the Robin Li fan club come out to get close to the object of their worship.

On a late morning in September, about 30 college-age kids wait expectantly outside the China World Hotel in downtown Beijing. When Li emerges from a dark blue sedan, the fan club mobs him, waving signs and screaming his name while Li poses for pictures with a tight, uncomfortable smile before darting into the building to rehearse his keynote address. "Robin Li is my idol," says Yan Huifeng, a student from Sichuan University in Chengdu. Liu Zhiqiang, a student at Beijing's Renmin University of China, says: "He is handsome and very intelligent and outstanding."

Like much about the 10-year-old company, the Robin Li fan club isn't quite what it appears to be. The exuberance, club members say later, was coordinated by Baidu, which Yan says flew her into town and paid for her hotel. The students all say they admire Robin Li, but their loyalty to the company he founded has its limits. "If I want to know about what happens abroad, I will use Google," says one of the students. "Baidu's information is influenced by the government so much."

The world knows Baidu as the search engine that kicked Google's butt out of China, with an assist from the Communist Party. The company has a 73 percent share of the world's largest Internet market by users, and has the fifth-largest market capitalization ($38.3 billion) among the world's pure-play Internet companies, trailing Google, Amazon.com, Tencent (an instant messaging and gaming company based in Shenzhen), and only narrowly, eBay. It's now 57 percent bigger than Yahoo!–and with significantly brighter prospects. Baidu "has the best business in the world," says Gene Munster, an analyst at Piper Jaffray. "It's hugely profitable, with massive growth ahead in the population of Chinese Internet users, and the government backing it up. Essentially it's a state-sponsored monopoly."

Baidu's stock price has more than doubled since January, when Google first disclosed that Chinese hackers had targeted its mail servers and announced "a new approach" to China, with the company saying it would no longer censor search results. The highly public stance ultimately led Google to begin redirecting all searches to a Google site in Hong Kong. This allows the company to avoid the strict censorship rules that Baidu and others in mainland China must follow, while also putting it at a major disadvantage in the huge Chinese market. "Every once in a while a gift is handed to you. We handed one to Robin," says Eric Schmidt, Google's chief executive officer. Schmidt argues that the playing field in China has always been unfairly tilted in Baidu's favor, though he goes out of his way to stay eligible for membership in the Robin Li fan club. "Robin is an example of a clever entrepreneur," Schmidt says. "He's navigated the conflicts within China–which are ferocious."

While Li has earned the grudging respect of Google execs, Baidu's tactics are a sharp contrast with the Google founders' sincere, if not always sincerely observed, slogan: Don't be evil. If crawling the Web empirically and without commercial bias is the moral duty of a search engine, Baidu is, at least in the eyes of its competitors, not a moral company. For years legions of advertisers have complained on Chinese Web forums that Baidu secretly penalizes the search rankings of websites that decrease their spending on Baidu. Archrival Chinese Internet company Alibaba, Jack Ma's Internet conglomerate that runs the Taobao e-commerce site and is 40 percent owned by Yahoo, says Baidu unfairly penalizes the search ranking of companies that accept ads from some Taobao merchants.

Robin Li disputes these allegations, saying the company never links search results and advertising. "We have a Chinese wall within the company" between the search and ad teams, he says, without irony. "These are all conspiracy theories. In reality we have no incentive to do that. Paid search is proven, and we are very confident we will be able to make

> "Every once in a while a gift is handed to you," says Eric Schmidt, chief executive officer of Google. "We handed one to Robin."

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Li poses with members of the Robin Li fan club, some of whom were flown in by Baidu

a lot of money by doing the right thing for users and advertisers." Many Chinese are nonetheless quick to believe the worst about Baidu: In 2008 the company quickly denied Internet chatter claiming it had taken money from Sanlu Group, a dairy producer that had sold milk powder tainted with the toxic chemical melamine, to keep the scandal out of search. At least six children died and more than 54,000 were hospitalized. Baidu has conceded that it has sometimes been too lax in policing its advertisers. In late 2008 the company acknowledged it had prominently listed ads from medical companies that weren't properly licensed, though Greg Penner, an early investor and Baidu board member who also serves on the board of Wal-Mart Stores, points out that no one in the Chinese search industry was vetting these advertisers.

One more denial: Baidu says it is not a kingdom built on Internet piracy, though music companies say its popular MP3 service allows users to download just about any song ever recorded for free. The recording industry sued in 2005, but Chinese district and appeals courts sided with Baidu, which says it's merely giving users the content they want by linking to popular music websites.

For many people outside China, these issues are minor compared with censorship. Like all Chinese Web companies, and Google's Chinese language site until this year, at the behest of the Chinese government Baidu blocks pornography or references to topics such as Taiwanese independence, the Dalai Lama, and the 1989 Tiananmen Square massacre. The practice is called zi lu, or "self-discipline," and Baidu does it well. Last year the company accepted one of 20 awards from the Internet Society of China, given for what the group calls "industry self-regulation."

Li, the fourth of five children born to factory-worker parents in Yangquan, a city of 1.3 million in northern China, received his bachelor's degree from the prestigious Peking University in 1991, and got a master's in computer science from the State University of New York at Buffalo in 1994. He has spent years in America, and speaks flawless English. His fidelity to China is nevertheless unquestioned. Li says that Baidu manipulates search results to obey the law of the land and that failing to comply would risk its license to operate in China and let down users and investors. "If the law clearly prohibits certain types of information, be it porn, or anti-government information, then I'm sure there's a reason for it," he says a few days before the Baidu World event, while sitting in the rooftop rock garden at his company's new headquarters, a 91,500-square-meter building (complete with a gym, yoga studio, and nap rooms) in the city's bustling Shangdi district. Of censorship broadly, Li says: "I'm an entrepreneur. I'm not a politician. I should not be in a position to make this kind of a call."

Instead, Li is focused on the future: expanding into games, e-commerce, and online payments, establishing a Hulu-like video site called Qiyi, and exporting the Baidu brand abroad. He says engineers are translating the site into a dozen languages. "I hope in ten years, Baidu will become a household name in 50 percent of the world. Sooner or later you will see a China-based company that really has a global impact and

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I think Baidu has a chance to become one of those companies. We should be able to compete on a global basis."

Before Baidu expands, however, it needs to answer an obvious question in an age when even the most transparent of Internet companies are struggling to maintain the faith of their users. "Why should I trust Baidu?" asks Rebecca MacKinnon, a senior fellow at the New America Foundation who writes about the Chinese Internet. "For the same reason nobody trusts the Xinhua news agency when it tries to expand into global readership, it's going to be very difficult for any Chinese companies that deal with content to get anyone to trust them outside of China."

This past June, Baidu hired Kaiser Kuo, an Internet pundit and former guitarist of the '90s Chinese metal band Tang Dynasty, to fill the new position of director of international communications. Kuo's role, in part, is to help tell Baidu's story to the world. "This is a company that looks a lot better on the inside than it does on the outside," he says.

Baidu says it's not evil, just misunderstood. And because it's expanding into fields like e-commerce and video games, and plans to get into markets outside of China, the company wants the world to know it better. And to trust it.

Key to the rollout and renovation of the Baidu brand is the selling of Robin Li. Once a Silicon Valley cubicle jockey earning around $45,000 a year at Infoseek, a forgotten portal from the Web's past, Li is now the second-richest man in China, with a fortune valued at $7.2 billion according to *Forbes* magazine.

Li is a poised but uninspiring public speaker and guarded in conversations with the press. Friends and colleagues say he is still essentially an engineer, and that his devotion to Baidu defines him. They tell stories of countless nights Li worked straight through, and of the times he fell asleep in his car after the drive home because he was too tired to walk to the front door. As for his faith in Baidu's future, there's this: According to public financial records, Li has never sold a single share of Baidu stock.

Recently, Li has begun cultivating an international profile. In July he attended Allen & Co.'s annual conference in Sun Valley, Idaho, for the first time and found a natural ally in Facebook founder Mark Zuckerberg. The two have talked several times, both executives confirm. On Nov. 15, Li will participate in a Silicon Valley public forum for the first time, at the Web 2.0 Summit in San Francisco.

Li's biggest boosters are his U.S. investors. A decade ago they backed an introverted search engineer and never anticipated he would take them on such a lucrative ride. "He had all the ingredients to be a good entrepreneur," says Hugo Shong, a founding partner at IDG Capital Partners, a firm with deep roots in China that invested $1.5 million in Baidu in 2000—a stake worth $170 million at Baidu's IPO in 2005. "We were worried about his marketing skills. He was so quiet."

Scott Walchek, an Alamo (Calif.)-based angel investor who put $1.25 million in Baidu and made hundreds of millions as a result, said that during the early years of the company he and other U.S. investors disagreed with Robin Li at almost every turn. "Nearly everything we said he should do, Robin disagreed. And he was always right."

Baidu is proudly Chinese, but its origins are in Silicon Valley. In 1998, Li's co-founder, Eric Xu, was a sales rep for a U.S. biotech firm who decided he wanted to make a documentary about



Baidu's new headquarters in Beijing's Shangdi district, complete with gym, yoga studio, and nap rooms

When Brin and Page visited Baidu, the company scheduled the meeting during a Chinese holiday when the office would be empty. That way the Google founders couldn't see how many engineers Baidu employed.

American innovation. Enlisting well-known Chinese American documentary filmmaker Ruby Yang, Xu got interview sessions with the British-American venture capitalist Michael Moritz and future Stanford University President John L. Hennessy. When Xu landed a chat with Jerry Yang, the Taiwanese born co-founder of Yahoo, he brought two friends to the taping: a fellow sales rep named Melissa Li, and her husband, Robin.

Xu conducted the interview while Li and Melissa looked on quietly. "I got inspired," Xu says more than a decade later. "I'm sure Robin got inspired, too, seeing an ethnic Chinese who created such a powerful company."

At the movie's debut on Stanford University's campus in 1999, Xu says Melissa pulled him away from the screening and declared that she would like her husband to be an Internet company founder.

Li was already a true believer in search. In 1996 he received a patent related to what he called link analysis, a way to rank search listings by the number of incoming links to sites. Stanford doctoral students Larry Page and Sergey Brin would separately come up with the similar PageRank algorithm. Inspired by Yang and pushed by Melissa, Xu and Li decided to use Li's research to build a search engine for the slumbering Chinese Internet market.

Looking for seed money, they brought their business plan to Bob King, a stalwart of the Silicon Valley investment community who put early money in Oracle and Intel and had appeared in Xu's documentary. Greg Penner, King's partner at the time, recalls that Li "wanted to create a major media company. That was his vision from day one. We weren't convinced that this was absolutely going to happen. We felt like if it did happen, he was the right guy to back."

With $1.2 million in seed money from King, Penner, and Walchek, Xu and Li left their wives in America and moved to a single hotel room near Peking University in Bejing. They stayed for over a year, working 15-hour-days in a nearby office. Later that year they scored an additional $10 million from IDG and ePlanet Ventures, an affiliate of Valley venture capital firm Draper Fisher Jurvetson.

In its early days, Baidu wasn't modeling itself on Google. Li and Xu were much more interested in being the next Inktomi, a U.S. firm that powered search on other Web portals and was eventually acquired by Yahoo in 2002 for $235 million. Rather than host an independent site, Baidu licensed its search index to Sina and Sohu.com, then the dominant portals in China, and charged them each time a user conducted a search. Busy copying Yahoo's portal business model, those companies didn't realize search's potential, concedes Charles Zhang, chairman and CEO of Sohu. "That's how Baidu captured this opportunity while [we] were not paying attention," he says.

Those relationships frayed immediately, however, since the number of search queries—and licensing fees owed to Baidu—were constantly growing. Two people involved in Baidu's early operations recall that Sina delayed a payment while demanding to renegotiate its search deal. Warming to Baidu's power, Li temporarily cut Sina off, infuriating the larger portal.

With its partnerships imperiled by its own success, Baidu began hedging and developed a website of its own. Finian Tan, then a Hong Kong-based partner at ePlanet, says he was so worried about the company's prospects that he contacted Jerry Yang, an ePlanet investor, and offered to sell Baidu to Yahoo for $40 million. It's not clear whether Yang remembered Li from the documentary shoot; he referred the matter to a Yahoo colleague, who did not respond. (Yang declined to comment for this story.) Baidu had no choice but to devote its energies to its own website. "We became Baidu.com because we were forced into it," Tang says.

By 2004, Baidu was allowing advertisers to pay to appear at the top of related search results, mimicking a model pioneered by a Pasadena (Calif.) company called Overture. Baidu was newly profitable and its traffic, along with China's Internet population, was skyrocketing. That year, Google contributed $5 million to Baidu's $15 million third round of financing, aiming to strike up a relationship with the Chinese startup. Although Google had offered search in Chinese from its servers abroad since 2000, the Baidu investment was meant to lay the groundwork for a possible acquisition and ward off the possibility that rivals could buy it, according to former Google executive James Mi, now a venture capitalist in Beijing.

From the beginning, Baidu and Google didn't trust each other. In late 2004, Brin and Page visited Baidu's offices during a visit to China. Xu says the Baidu team scheduled the meeting during a national holiday when the office would be empty, so the Google executives couldn't see how many engineers Baidu employed. Brin and Page declined to eat the Subway sandwiches Baidu served for lunch. (James Mi recalls that this was because the Google founders had recently gotten sick from uncooked food in India and were being cautious.) When Brin asked whether the Baidu logo was a dog's paw, Li corrected him brusquely. (It's a bear paw.) "We respected Google, but as a company we were competitive and we wanted to make sure they respected us," says Xu, who left the company in late 2004 and founded a venture capital firm that specializes in biotechnology.

As Baidu filed to go public in July 2005, acquisition and investment offers poured in. The story of those offers has not been told before. According to several people familiar with the submissions, Masayoshi Son, founder of SoftBank, the

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Japanese Internet giant, wanted to keep Baidu private and offered to invest $100 million at a $1 billion valuation. Yahoo and Microsoft made acquisition offers at a little over $1 billion. Google kept a close eye on the proceedings. Its China-based brain trust wanted the U.S. search company, valued at $27 billion in its own 2004 IPO, to bid $2 billion for Baidu. Google management in Mountain View, Calif., ultimately made a $1.6 billion bid.

Baidu's board of directors was split, with the U.S. partners of ePlanet's affiliate, Draper Fisher Jurvetson, aggressively lobbying for the sale to Google. "It was certainly a very stressful period for me," Li says. "During the day I would talk to potential investors and tell them why they should buy Baidu stock. At night, I picked up the phone and called the directors and explained why they shouldn't sell the company so early."

Weighing the possibility that the impassioned Li might resign and scuttle an acquisition, the board voted unanimously to go public. Asad Jamal, the founding partner of ePlanet and a Baidu board member, thinks a $2 billion bid would have cemented an acquisition. "I personally think that was a missed opportunity for Google," Jamal says.

Baidu stock hit the Nasdaq on Aug. 5, 2005, and jumped from $27 to $122 in a day, briefly valuing the company at more than $4 billion and showering hundreds of millions on Baidu's early investors. News of the offering also imprinted Baidu on the minds of Chinese consumers and advertisers, and made Li China's first billionaire Web prodigy.

Google responded to Baidu's success by hiring noted computer scientist Kai-Fu Lee from Microsoft and opening a research and development center in Beijing. "At that time I had concerns. Google had a lot of money," Li says.

Yet Google never materialized as a threat, for reasons that no one can agree on. What's clear is that Google's China service was mysteriously unreliable, particularly when the Chinese government was angry with the U.S. Google also documented several instances when it was the victim of what's called domain name system poisoning; users typed in Google.cn and found themselves at Baidu instead.

Some Google executives privately say they think the Chinese government was never going to let Google succeed. MacKinnon, at the New America Foundation, says the opaque Chinese regulatory system makes it difficult to prove there was official discrimination. "Did Google face a very poisonous atmosphere in China? Sure," she says. "Whether this was the result of top down policy or the fact that Baidu's government relations were simply better is impossible to say."

In November 2009, Kai-Fu Lee announced he was leaving Google to start a Web incubator, throwing the company's regional leadership into disarray. Two months later, Google suffered the attempted hack on its e-mail servers, and after a debate in which Schmidt tried to persuade Brin and Page to stay in China—and was overruled by the founders—Google relocated its search servers to Hong Kong, declared itself not evil, and departed the field. "We understand from a commercial standpoint that this isn't the ideal state of affairs to compete in that market," says David C. Drummond, Google's chief legal officer. "But after a couple of years observing these content laws, we decided they weren't consistent with our values."

Google may have lost its battle with the Chinese government, but it was defeated first in the marketplace. Li says his original impulse when facing off against American competitors was to downplay Baidu's heritage as a Chinese company, because "in most consumer's minds, Chinese products are low quality." But in a widely televised ad campaign that referenced a popular Hong Kong film, Google was depicted as a clueless Caucasian who could only interpret a complex Chinese sentence in a single way. A scholar representing Baidu handles the sentence correctly; the Google character ends up spitting blood. "It was the easiest way to tell them Baidu knows Chinese better," Li says of the ad.

For years, Baidu really was better able to parse sentences in Chinese. Baidu also put more sales people on the ground to talk to advertisers, and demonstrated a better grasp of Chinese tastes. Baidu's home page has 11 links, in underlined blue, to various services such as Baidu Knows, a Q&A service; Baidu Post-Bar, a popular bulletin board; and Baidu Encyclopedia, a made-in-China alternative to Wikipedia. Like Google, Baidu is a verb: To search, users click on a box that says "Baidu It." "Robin took the best of everything that was happening in the U.S. at the time and added Chinese characteristics," says U.S. venture capitalist Tim Draper.

Baidu MP3 proved a particular draw for Chinese Internet users, and no wonder, since it helps users download for free.





Li (fourth from left) with his crew in 2000, and jotting notes in a hotel suite Baidu rented as an office in 2002

BAIDU

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In its IPO prospectus, Baidu said its music service accounted for about 40 percent of its traffic. (It now claims that number is down to around 5 percent as interest in digital music has waned.) Baidu says it is trying to reach an accommodation with record labels and in 2008 hired Catherine Leung, a former executive at Universal Music Group, to lead the discussions. Still, Li says piracy is not his problem. "If [users] are looking for certain type of content that is publicly available, we cannot say, in order to make sure record companies are happy, let's completely block out this type of service. We choose not to do that." Sohu CEO Zhang says such an argument "is the official line. They're not conducting evil, just spreading it." Of course, Sohu also links to free tunes, and Zhang says he won't clean up his act until Baidu does. "We will just follow the big fish," he says.

Google, because of its need to forge strong relations with the entertainment industry in the U.S., could never facilitate copyright infringement in the same way. Only in 2009 did Google introduce a free, ad-supported music service in China, in conjunction with music labels. By then it was far too late. Baidu was the fun option for the masses, while Google was viewed as the search engine for the coastal intelligentsia, who admired its brave resistance and then loud rejection of government censorship requirements. Robin Li heard about Google's threatened withdrawal from China in his car on the way to the office, via a congratulatory text message from a friend at a Chinese Web portal. "I certainly don't agree with the way they framed the issue," he says of Google's exit, noting that despite the censorship, there are millions of Chinese websites only because there is a search engine to help people find them. "There are people who don't like us. I think for a service with hundreds of millions of daily users, it's probably normal, especially when you have a competitor that claims they are anti-government, that they don't like censorship."

A few hours after greeting his fans, Li addressed the Baidu World conference. He spoke in Chinese to an audience of developers and Communist Party officials, and announced that Baidu would start placing games, videos, and maps directly within search results. Li then praised Wan Gang, China's Minister of Science and Technology, for articulating the need for such functionality.

It was a moment that revealed a truth rarely visible to non-Chinese. Despite the perception of Baidu as a preferred vendor of the Communist Party, company executives say they must constantly curry favor, particularly as the Party asserts greater control over the media. "One of Baidu's biggest challenges is keeping its copybook clean with the government," says Duncan Clark, chairman of BDA China, an investment advisory and consulting firm in Beijing. Kaiser Kuo puts it less delicately: "We get smacked as hard as anyone."

The blows, particularly in the last two years, have left several marks. In November 2008, government-operated China Central Television aired several in-depth investigations about Baidu surrounding allegations that the company earned millions on ads from unlicensed medical providers, and prominently displaying these ads when users typed health-related queries. The first story ran on Li's 40th birthday, timing that no one at Baidu dismissed as coincidental. The following quarter, Baidu boosted its ad spending by 41 percent, with the bulk of the increase going to CCTV. Few Chinese Internet watchers thought it was a coincidence when the negative coverage ceased.

An Alibaba spokesman says of Baidu: "These guys are like hoodlums." Baidu's communications chief responds by calling Alibaba "whiny little bitches."

In August the Xinhaua News Agency announced it was developing a competing search engine in conjunction with China Mobile, one of the country's state-owned mobile carriers. In September the *People's Daily*, the Communist Party mouthpiece, appointed a former Olympic Ping-Pong player to run its new search engine, Goso. The idea of government-backed entities developing something as technologically complex as a search engine doesn't concern Baidu much. To observers familiar with how business is conducted in China, though, the announcements were a strong message aimed at Baidu: Don't get too comfortable. "The experience with Google made it very clear to the government that sometimes a commercial company will not play by the rules," says Mark Natkin, managing director of Marbridge Consulting in Beijing.

With Baidu assured of nothing from the government, and Google fading from view, Baidu is now fighting Alibaba and Tencent in a three-way skirmish to be China's preeminent Internet company. Alibaba has blocked Baidu's search engine from cataloging products from its marketplace and is developing its own shopping-oriented search engine. Tencent has been cherry-picking engineers from Google and Baidu and vowing to improve its Soso.com search engine. "It's real war," says Tom Melcher, a U.S. entrepreneur who has lived in China for eight years. "It makes Ellison vs. Gates look tame." Proving the point, John Spelich, an Alibaba spokesman, said of Baidu in August: "These guys are like hoodlums." Kaiser Kuo responds by calling Alibaba execs "whiny little bitches."

During rehearsal the night before his Baidu World speech, Li is asked whether he's satisfied that Baidu has struck the right balance between loyalty to the Chinese government and service for its users. "At the end of the day," says Li, "if users don't find what they want, they won't use you. If they find what they want, they come back again."

Of course, if you believe Baidu has always had a unique home-field advantage over rivals like Google, that proposition has never been seriously tested. With other Chinese Internet firms rushing to build search engines, and with Li's ambitions to move overseas where Western rivals are entrenched, Baidu is about to face more serious competition than ever before. The world's Internet users will finally get to decide for themselves whether they can really trust Baidu. Ⓑ

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The Pistachio King and the POM Queen



They own this painting, *Muse in a Theatrical Landscape*, by Hermann Albert

Lynda Resnick built POM Wonderful into a $100+ million business

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Stewart Resnick is the largest pistachio grower in the U.S.

Why is everybody suing such a nice, generous couple?

By Susan Berfield
Photographs by Bryce Duffy

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On an unexpectedly rainy October day in Los Angeles, Stewart Resnick looks out the window of a third-floor conference room and shrugs. It's midway through California's biggest-ever pistachio harvest and the rain is yet another reminder, should anyone need it, of how important water is to his business. He helps himself to a half a vegetable wrap and a bottle of Fiji Water—one of the four big consumer brands Resnick owns—and takes his place at the head of the table, where senior executives of his private company, Roll International, have gathered to discuss how to sell 300 million pounds of pistachios.

Resnick, 72, is short, trim, and tanned, dressed in jeans and a blue-and-white striped shirt. He and his wife and business partner, Lynda, are quintessential Beverly Hills billionaires, with a sumptuous mansion and a new $54 million pavilion named after them at the Los Angeles County Museum of Art. They diverge from the Beverly Hills norm, however, in this respect: The source of their wealth is one of the biggest farms in California's agricultural heartland—188 square miles of land, a holding four times the size of San Francisco—aptly named Paramount. There they grow oranges, almonds, pistachios, and pomegranates; their Pom Wonderful juice launched the pomegranate superfood craze.

Dave Szeflin, who manages Paramount's processing plant, throws a bag of raw pistachios on the table and sits down heavily. The plant has been operating 24 hours a day for the past 21 days.

"Well, the growers should be happy," says Resnick.

"The growers should be very happy," says Szeflin.

"They should be beyond happy—ecstatic," says Resnick.

Szeflin tells him a grower they both know stopped by the plant to say just that. "He said, 'The sound of money is when a harvester goes next to a tree in an orchard with 7,000 pounds of pistachios and shakes it. That sound, when the pistachios hit the catch frame, that's the sound of money.' "

Everyone in the room knows that sound.

"It's like a Vegas slot machine," says one executive.

"Record prices and record deals," says Szeflin.

"It's good for Stewart. He's got both," says another.

The giddy, money-really-does-grow-on-trees attitude in the conference room belies trouble. In the past few months the Resnicks have been hit with two major legal challenges that have exposed them to unflattering scrutiny. There is a floor at Roll headquarters just for the lawyers preparing to fight on behalf of the Resnicks, in courts of all kinds and for many years to come.

The first suit, filed by several environmental groups and water agencies, threatens a crucial element of Paramount's business: its sizable stake in an enormous underground water bank in the San Joaquin Valley. The second, brought by the Federal Trade Commission, accuses the Resnicks of making false health claims about Pom Wonderful.

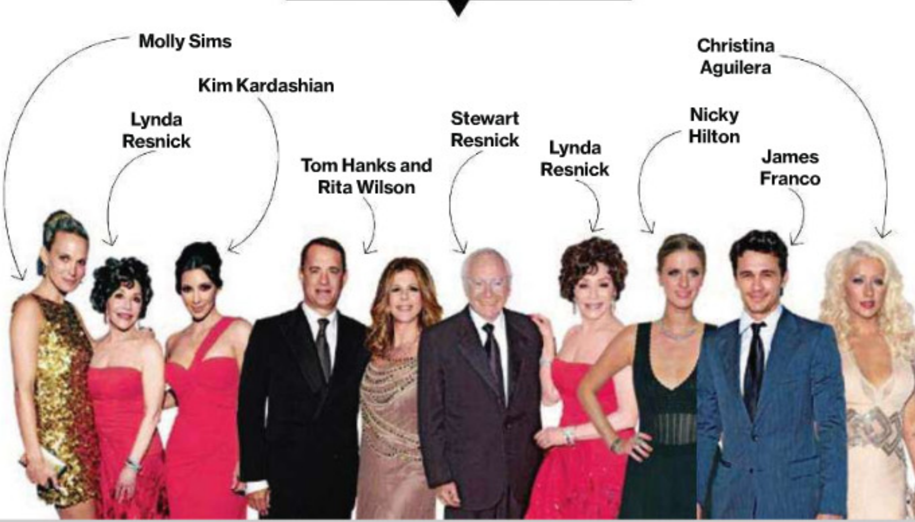
Stewart calls the environmentalists' lawsuit "a nuisance" and the FTC's actions "foolish." But if the allegations are proven, they may affect businesses worth $2 billion. Already, they have begun to undermine an image of beneficence that Lynda, in particular, has worked hard to cultivate: The Resnicks are generous philanthropists and boast that Roll's products either "are good for you or make you feel good."

All of which may help explain why Stewart Resnick agreed to give *Bloomberg Businessweek* a rare look inside Roll International, which includes Fiji Water, the bottled water shipped from the remote South Pacific island; Teleflora, the flower delivery service; and Suterra, an environmentally sensitive pesticide. To hear Resnick tell it, though, he's not concerned about public perception. "If I think I'm right, I don't care what people say. It's their problem," he says. "Lynda can't take negativity. I told her, 'There's just one thing in life you have to understand, and then nothing will bother you: If you're successful, no good deed goes unpunished.' "

The Resnicks are the biggest citrus, pomegranate, almond, and pistachio growers in the U.S. They are also processors, buying from other farms, and their Paramount plant, set in the fields of the San Joaquin Valley, 140 miles northeast of Los Angeles, cleans, roasts, and packages 60 percent of the domestic pistachio crop, or about 30 percent of the pistachios in the world. With a commanding share of the $2 billion global market and the advantage of being both a buyer and a seller, Resnick puts enormous upward pressure on the price of pistachios.

Pistachios require a modest but regular supply of water—a commodity sometimes so hard to come by in the Central Valley that it can dominate all other discussions. Season after season, Resnick has outwitted the weather, largely because of Paramount's water bank, which is the biggest in America, if not the world. It occupies 32 square miles in Kern County, making it larger than Hollywood and Beverly Hills combined; it extends across the main highways that run through the San Joaquin Valley and alongside the California aqueduct. The bank itself is a network of 70 man-made ponds, a six-mile-long canal, and 33 miles of pipeline that captures rain and snowmelt from the Sierra Nevada range and can be fed by water purchased from the federal and state governments as well as local sources. (In very wet years, the bank can take water from the Kern River,

Opening night at the Resnick Pavilion in L.A.



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Paramount's state-of-the-art plant handles 60 percent of the U.S. pistachio crop



The farm, 188 square miles, grows pistachios, almonds, pomegranates, and citrus fruit

Lost Hills, Calif.

too, which runs through it.) Within days the water percolates through a layer of sand into an aquifer; 85 wells pump out water when it's needed.

Water banks are eagerly endorsed as a public resource but are increasingly divisive as a business proposition. In California, water means power and wealth: It is dammed and diverted and transported hundreds of miles to let great cities (and great pistachio orchards) blossom in bone-dry places. As a changing climate makes the American West increasingly arid, Resnick's water bank may someday be more important than his orchards. "The value of the Kern Water Bank will only increase as uncertainty over our water situation grows," says Peter Gleick, co-founder of the Pacific Institute, a nonpartisan research organization in Oakland.

In 2007, before three dry years, the bank held a total of 1.5 million acre-feet of water, or 490 billion gallons, an astonishing amount in a county that gets just six inches of rain in a typical year. But you could drive right over parts of the bank and not know it. The land is yellow and brown, covered in scrub brush, dry grass, mesquite, tumbleweed, and sage.

On a recent morning, the sound of rushing water booms in the ordinarily quiet landscape. One member of the bank is depositing 10,000 acre-feet of water—the first time any of them has made a deposit in three years—and it is being transported through the Kern Water Bank Canal into some of the ponds. As they fill, herons, coots, egrets, even a pheasant or two gather.

The Kern Water Bank has six members in all, but Paramount is the biggest, with a 52 percent stake. The five others are water districts and agencies serving farmers and homeowners. Each member maintains an underground water account, storing water in wet years, drawing it down in dry ones, and selling it whenever they choose. "We're like Bank of America," says Jonathan Parker, the general manager. "We hold the money and give it back to the participants when they want it." Except almost anybody can open an account at Bank of America; only the members can deposit water in the Kern Water Bank. Resnick compares it to insurance. "It lets us do things without worrying about the ups and downs." Some of those things include nearly doubling the number of Paramount's pistachio trees.

Owning the water bank has other advantages, too. During the wet years from 2000 to 2007, California put in place a water trading program that was supposed to satisfy environmentalists trying to reduce pumping to protect smelt and salmon as well as farmers wanting water for irrigation. The state sold water from the Sacramento-San Joaquin River Delta to farmers at very good prices, and Paramount bought and stored billions of gallons. "You just had to ask for how much you wanted," says Jonas Minton, who worked for the Water Resources Dept. at the time and is now an adviser to the Planning and Conservation League, an environmental group that earlier sued and settled with the water bank. Then the state periodically bought back water, at much higher prices. The deal was open to anyone, but not everyone had water to sell. "[Paramount was] the single largest beneficiary of the scheme," earning tens of millions of dollars, and quite possibly more, Minton says. William Phillimore, who has overseen Paramount's water program since the late 1980s, says the company was "happy to support an effort that was intended to help the environment" and that its water "was among the least expensive" available to the state.

A lawsuit brought in July by three environmental groups and two water agencies claims that in an era of growing scarcity, such a tremendous resource should not be privately owned. They are challenging a broad set of policies and decisions made by California's Water Resources Dept. in 1994, one of which was the transfer of the Kern Water Bank

OPPOSITE PAGE: AP PHOTO; BEIMAGES; CORBIS (2); GETTY IMAGES (2)

The Kern Water Bank in the San Joaquin Valley



from state ownership to local groups led by Paramount. Back then, Paramount and other agricultural water users in Kern County were negotiating with the state for more water, claiming urban areas had been given undue preference during the drought of 1991. "We managed to get through the year, but it took a lot of hard work," says Phillimore. "We didn't want to go through that again. That's when we first thought of acquiring what the state was trying to develop. They were generally screwing it up ... and they wanted to get rid of it. We were kind enough to take it off their hands."

State officials turned over the water bank–which had cost about $74 million to develop but was not yet in use–to the Kern County Water Agency, which in 1995 passed it to the group that operates the bank on behalf of Paramount and others. In exchange, the new members of the bank gave up their claim to state water allocations, which California may or may not have been able to deliver. Resnick says those rights could be worth $200 million today and that the new owners spent $35 million to make the bank operational. "We paid for it, we built the infrastructure. We took a big risk," he adds.

"Paramount and local water groups have been ruling the roost for a long time. They've divided up the spoils," says Adam Keats, a lawyer for the Center for Biological Diversity, the leader of the group suing to return control of the water bank to California. "They have their own philosophy and theory about how the world should work, which involves them getting very rich on our resources," he says.

There are other lawsuits, too, demanding more accountability from the water bank. A suit brought by a rival processor, Ali Amin of Primex Farms, accuses Paramount of selling water cheaply, though profitably, to lure away a grower crucial to his business. The other, filed by a water storage district that lies directly south of the water bank, blames the heavy pumping out of the aquifer during the past three years of drought for lowering the water table and drying up the wells of its residents. Phillimore, who is also chairman of the Kern Water Bank Authority (which operates the bank), says it's the district's own mismanagement that caused the bank's neighbors to run short of water.

Someone else might tread lightly here, realizing that whatever the merit of each specific charge, together they are symbolically powerful. Not Resnick. Over lunch in the Orchard, Roll's new light- and art-filled cafeteria, he says of Amin, whose name he won't even mention, "He wanted to be a major player and he continues to have a lot of animosity and he'll never change." And the environmentalists' lawsuit? "They don't know what they're talking about," he says as he tucks into a grilled salmon salad. "The ones who are complaining are saying, 'You have the water and we want the water.' Well, that's great. There are guys in Beverly Hills who have land and I want that land. Maybe they bought it for $10,000 and now it's worth a million and I'd like some, give it to me."

What would happen to Paramount if the environmentalists were to prevail and it loses the water bank, the war chest it has deployed to such great effect for the past 15 years? "I don't know how we could lose it," Resnick says. "We bought it. We own it." Without a reasonably priced supply of water, of course, Resnick could find his domination of the pistachio market compromised.

When a metal shaker clamps on to a pistachio tree, the ground shakes. There's a draft of air, and in one violent burst close to 150 pounds of nuts come flying off the branches into a huge catcher. The whole thing lasts five seconds. This year, Paramount has had 100 of these machines operating day and night for eight weeks.

"It's hard to believe those fields. When you fly over the west side [of the Valley], as far you can see it's basically all our property," says Resnick, who sometimes enjoys the view from his own plane. The orchards lie about 60 miles north of the water bank. "I first bought some land in the late 1970s as a hedge against inflation," he says. It could have been a suburban office park for all he cared. "I thought I'd buy a piece of land for my kids, and hopefully it would go up in value." (The Resnicks have five children from previous marriages, but none together.)

Stewart grew up in New Jersey and came west with his family during California's golden age in the 1950s. He was at UCLA when his father lost everything. "He was a very smart guy, but he was an alcoholic and a compulsive gambler," says Resnick. "Other than that, he didn't have any vices." He laughs. "My father was a great example of what not to do, quite honestly. He had been middle-class, he had a local bar, and then he was poor. I realized I didn't want to go backwards." Resnick started his first business, a janitorial services company, while in law school and sold it in 1969.

Soon after, he married Lynda, his second wife. They met when she made an advertising pitch for a small business he had invested in. She had grown up a child of privilege on the East Coast; her father later moved the family to Los Angeles and achieved some fame as the producer of the cult classic *The Blob*. Lynda had been on television as a kid and considered becoming an artist, but instead started her own ad agency at age 19. As she likes to say of her first encounter with Stewart, "I never got the account. But I sure got the business."

The Resnicks began buying companies, starting with Teleflora, which they built into the nation's largest flower delivery service and then, in 1985, the Franklin Mint, purveyor of commemorative coins and other kitsch. Both were

KERN WATER BANK

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good matches for Lynda's marketing skills. She famously paid $211,000 for Jackie Kennedy's fake pearls, and then the Mint went on to sell $26 million worth of replicas. More notoriously, in 1998 the Mint was sued by The Diana, Princess of Wales Memorial Fund for selling unauthorized dolls; the Mint won and then accused the Fund's lawyers of malicious prosecution. The case is still in the courts. Meanwhile, the Resnicks sold the Mint in 2006, after eBay had begun taking its business away.

In the mid-1980s, they expanded their land holdings significantly, and cheaply, by buying orchards that Superior and Getty Oil were unloading. Now they had oranges, pomegranates, almonds, and pistachios. Lots and lots of pistachios. "We had enough that we could be the market leader," Resnick says. "Our intent was always to be the leader."

California and Iran are the two major pistachio producers in the world. In Iran, farmers have been planting the trees, which take nearly six years to produce a commercial crop, for centuries. In California, they had been doing so on a small scale for just a few decades. Resnick saw an unlikely opportunity: a relatively new American industry that he could shape into a global competitor.

One of Paramount's strategies is to maximize its profits as a grower even if it means minimizing its profits as a processor. That has changed the economics of the Valley, making it better for the farmers and much worse for rival processors such as Amin. As Paramount has proven its ability to sell more pistachios at higher prices, farmers have been growing more. This year, in part because Iran is recovering from a drought, California is likely to be the world's top producer.

An even bigger Paramount in an even bigger industry is an unsettling prospect for some in the Valley. Resnick calls them the "diehards"; they are the ones who are still angry that he killed their cooperative three years ago. As he talks about those days his voice hardens. He's agitated, as if he still can't believe how he was treated. "It was one man, one vote," he says. "A person with 20 acres had the same vote as we had with 30,000 acres." He suffered other perceived injustices. "The head of the co-op, in the 10 years we were in it, she came down to visit me once."

Paramount filed a lawsuit against the co-op, claiming it was violating Resnick's freedom of speech. The legal fight distracted the co-op and drained its resources, and when a routine vote came up, the members decided to disband. Resnick is blunt: "The commission was wasting my money and wouldn't change. So eventually we eliminated it and went on our own, and it's really much better. ... You cannot run a business democratically."

There are other things the Resnicks are doing on their own now, too, most of which farmers don't usually try. Lynda and the Paramount staff turned their pistachios into a boutique product with a brand name, Wonderful, a premium price, and an aggressive advertising campaign called Get Crackin'. Last year, Levi Johnston, the on-again, off-again member of Sarah Palin's clan, appeared in one of the television spots. A dominatrix starred in another. Sales nearly doubled afterward.

Paramount also cut out the middlemen that stood between it and the supermarkets that sell its Wonderful pistachios. Now, Paramount's merchandisers arrive at Krogers and Safeways and Supervalus around the country in Toyota Priuses emblazoned with the Get Crackin' logo and set up their own promotional stands right in the stores. "We've learned that if anything is important enough, we're better off doing it ourselves," Resnick says. Lynda puts it more brightly: "What we're saying is: 'The Resnicks planted these trees, grew these trees, loved these trees, processed their nuts, and sent them to you.' We're a mom-and-pop operation." Really what they've done is build a farming empire by bringing together two parts of California that are as distinct in psychology as they are in geography: Hollywood and the heartland.

Lynda, who declines to disclose her age, is petite and formidable, with a brassy voice and a stand-up comic's sense of timing. She is sitting on a silk couch in the music room at Sunset House, her 25,000-square-foot beaux arts mansion. It is a place of regal proportions—"Lynda says we're too short to live here," Stewart jokes—and grand gestures. The music room is glazed in a shade of blue that complements the sash in an 18th century French painting by François Boucher, *Leda and the Swan*, which usually hangs over the fireplace. The dining room seats 22; the foyer can hold 100. At one end of the drawing room sits a larger-than-life-size marble sculpture of Napoleon. The grounds are expansive, with a lush lawn and sculptures of sheep on one side, a pool and "victory garden" on the other. They've lived here for 34 years. "It's not home, but it's much," she and Stewart like to joke.

Selected pieces from their Old Masters art collection, including a portrait of a young Marie Antoinette, are on display at LACMA's Lynda and Stewart Resnick Exhibition Pavilion in a show titled "Eye for the Sensual." In the week preceding the opening, Lynda gave several tours, saying of Marie Antoinette, "A great deal of her bad press was manufactured by her enemies. She needed a better publicist. And she certainly needed a stronger husband." Tom Hanks and James Franco were among the 1,000 people who attended the fundraiser honoring the Resnicks. Christina Aguilera performed.

That was Saturday night. On Monday morning, Sept. 27, the Federal Trade Commission went public with its complaint against the Resnicks. After failing to come to terms over a settlement, the FTC sued them both, as well as the president of Pom Wonderful, for making deceptive claims about the health benefits of pomegranates. The allegations cut to the core of the Resnicks' business strategy and identity: If you've consumed a pomegranate martini or frozen yogurt lately, or think pomegranate juice is good for your heart, or will help with prostate cancer or even erectile dysfunction, it's probably because of Lynda. She read the lore about the pomegranate's supposed powers. She spent $34 million on dozens of research projects and clinical trials to try to prove them. She fashioned an entire



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marketing strategy—and public persona—based on the assumption that she had proof. She wrote a book, touted as her "secrets to marketing just about anything," and titled it *Rubies in the Orchard*. She calls herself the Pom Queen.

In its 25-page complaint, the FTC highlights some of the more brash ads Resnick has run: "Drink to prostate health. Sometimes, good medicine can taste great," began one in *Prevention* magazine; "I'm off to save prostates! Man by man, gland by gland...," read another in *Men's Fitness*. Lynda is quoted on Martha Stewart's show saying, "It is the magic elixir of our age and of all ages." In an interview with *Newsweek*, she winked at a young reporter and told him pomegranate juice is 40 percent as effective as Viagra. "Not that you need it. But—couldn't hoit!"

Lynda may have made the pomegranate juice market, but she didn't have it to herself for long. All of the big juice companies have come out with pomegranate drinks. Pom Wonderful had sales of $165 million in 2006, although the Resnicks say it has never made money for them. They did not disclose more specific numbers. Their fresh pomegranates do: They expect to sell 3 million cases this year. The Resnicks claim that many of these other juices, priced lower than Pom, don't have much pomegranate in them. They've sued Coca-Cola (which owns Minute Maid), Pepsi (which owns Tropicana), Welch's, and Ocean Spray for false advertising. Coca-Cola won its case on summary judgment, though Pom is appealing. A jury found that Welch's deceived buyers but didn't award Pom damages; Pom is appealing that case, too. The Tropicana trial is under way. Lynda suggests the FTC is too close to the big beverage companies and went after the Resnicks in retaliation. "What's motivating them? Is it our competitors, who have all these lobbyists there?" she asks. Pom, she says, doesn't have lobbyists.

The case against the Resnicks will be heard by an FTC administrative law judge in May; the couple expect to appeal to a federal court after that. They have already filed their own suit against the FTC, claiming that preventing them from publicizing the results of their studies violates their right to free speech. "We are consumed with doing good," says Lynda. "That's why this Pom stuff is so ridiculous. Please. We are fruit. Hello? Why do we need thousands of people in a 20-year trial for fruit? They do it for drugs because drugs kill people, or potentially harm them."

Lynda Resnick

> "We are consumed with doing good. That's why this POM stuff is so ridiculous. Please. We are fruit. Hello?"

Stewart, a prostate cancer survivor who takes two pomegranate pills every morning, is no less adamant, but he isn't likely to describe pomegranates as a magic elixir of all ages, either. "Could we have been over the gray line a few times? There's an argument," he says. "But what they want to do is silly. Do we believe the science? Absolutely. And do the doctors believe it? Absolutely. Now, do we have a 5,000-person double-blind, placebo-controlled 12-year study on prostate cancer? No. How could we? But believe me, there is real evidence this is helpful. By not saying so, it's wrong. Seriously."

"I love using Pom research as an example of how easy it is to design elaborate studies to give you the answer you want," says Marion Nestle, professor of nutrition, food studies, and public health at New York University. "They spent $34 million proving that pomegranate juice has antioxidant activity. I could have told them that for free. All fruits do. What the studies don't do is compare the effects of pomegranate juice to orange juice, for example. They wouldn't get the answer they want if they asked that question."

As luck would have it, a new $10 million ad campaign for Pom, its first on television, had been scheduled to debut the last week in September, just as pomegranate season began. The series of three commercials is a dramatic shift in style and substance: Quiet, dreamy, and provocative, they hype the centuries-old idea that pomegranates are aphrodisiacs. One of the spots shows a naked Eve, played by Sonja Kinski, being caressed by a snake as she reaches for a bottle of Pom Wonderful. A breathy voice intones, "Some scholars believe it wasn't an apple, but a ruby-red, antioxidant-rich pomegranate with which Eve tempted Adam."

"The FTC was after us, and we were searching for a new concept for a long time," says Lynda.

Back at the Orchard, lunch is over. Stewart pushes his empty salad bowl aside and considers his four-decade-long partnership with Lynda. "It's good to be king," he says, "but you know what? It's also better to be queen."

At Roll, the Queen wants to spend more money on marketing. Lynda tried for years to persuade Stewart to launch an ad campaign for their pistachios. It took a salmonella scare and a recall in 2009 for him to agree. This year's $20 million Get Crackin' commercials, featuring eight celebrities, began airing on Halloween eve. "You want to go with people who are part of pop culture," Lynda says. "You wouldn't want balloon dad. That was pathetic." You would want Snooki, the star of *Jersey Shore*, though. "She just sums up reality TV, and reality TV dominates our lives." You'd want Rod Blagojevich, the disgraced Illinois governor, too. "He's animated. He's an avatar of himself," says Lynda. Her next big effort will be marketing Paramount's seedless mandarins, which she's branded as Cuties.

On the bright side, then, there is Snooki, Blagojevich, Eve, a record crop of pistachios, and a growing share of the global market. Stewart Resnick may be right that success is always punished, or it may be that broken systems are sometimes fixed at the expense of those who understand them best. One of the most telling comments comes from an unexpected source, Keats, the lawyer for the Center for Biological Diversity. "The Resnicks are acting rationally," he says. "The system is rotten. It's a mistake to think it's just the Resnicks. They're particularly adept at exploiting the system. But anyone in their situation would do the same."

The Resnicks are looking ahead. Lynda says she may focus more on the couple's philanthropy. "We're going to go through some hard times in America," she says. "I get maudlin. I do. I know too much." The couple spends summers in Aspen, where Lynda is a member of the Board of Trustees of the Aspen Institute, a self-described neutral venue for discussing and acting on critical ideas. "Every great thinker comes out there and tells us what's going on in the world," she says. "By the end of the summer, I want to kill myself."

Stewart says he wants to do nothing but what he's already doing. "I have a great time," he says. "If something goes wrong, it might be a headache, but it's not going to affect the quality of our life. Also, I believe that luck evens out. So that's why if I go to Las Vegas and lose, I don't mind. Seriously, if I win too many times, I get nervous." B

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The Best Business Schools 2010

Working through the post-crash hangover, B-schools put new emphasis on job placement—and some hard lessons learned. By Geoff Gloeckler

Jack Oakes didn't like what he was seeing. As director of the Career Development Center at the University of Virginia's Darden School of Business, Oakes had watched the Great Recession choke off his students' job opportunities. The outlook was no better for the MBA Class of 2010. By the end of February only 64 percent of students reported having received a job offer, even worse than the recession-era low of 69 percent in February 2009 (and well below the 81 percent in pre-crash 2008). In the world of elite MBA programs such as Darden, where graduates have come to expect multiple six-figure offers, this qualified as a disaster. Something had to be done.

On Mar. 16, Oakes asked three of the school's best-known and longest-tenured professors to send an e-mail to alumni explaining the crisis and asking for help. The subject line: "A Darden Call to Arms." "It might not have been war, but for many of these students who were still looking for jobs, it sure felt like it," Oakes says.

Within hours, dozens of Darden alumni responded with job leads.

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'The financial crisis revealed fault lines that no business school is structured to address. When it is clear the institutional context of business has failed us, most business schools are isolated from the domains of knowledge necessary to redress those failures, such as the environmental and policy schools of their own universities. When we most need graduates of great character capable of becoming consequential leaders, we often turn out narrow technocrats. We have an obligation to fix these structural flaws.'

—Blair Sheppard, Dean, Fuqua School of Business, Duke University

3:2

The ratio of men to women at Wharton, the school with the largest percentage of female students

By graduation in May, 77 percent of the class had job offers; three months later the figure reached 87 percent. "It was something we had never done in the past," Oakes says. "We didn't have to. But things are different now."

Because the financial crisis killed or downsized some of the biggest MBA employers, including Bear Stearns and Lehman Brothers, the B-school job search has grown far more arduous. That's clear from *Bloomberg Businessweek*'s 2010 ranking of the top full-time MBA programs. Consider this contrast: Three months after graduation in 2007, only 4 percent of grads at the 30 top U.S. schools did not have a job offer. That figure has risen to 12 percent, and at some schools it's more than double that. Even top schools lost ground. At No. 1 University of Chicago Booth School of Business, 9 percent of students were jobless at the three-month mark, vs. 2.4 percent in 2007, while No. 3 University of Pennsylvania Wharton School saw its three-month unemployment rate more than triple, from 3.9 percent to 13 percent, over the same period.

No longer can students rely on the traditional on-campus recruiting process. More than 40 percent of B-school career services officers saw a decline in on-campus visits this spring, according to the MBA Career Services Council (CSC). And when companies do come to campus, instead of having a dozen positions to fill, they might have two or three. Starting salaries among all MBAs surveyed by *Bloomberg Businessweek* have dropped nearly 6 percent, from an average of $104,500 in 2008 to $98,400 this year. And students' plans are changing, with many settling for lesser positions. More than half of those surveyed expressed concern about the job market. "I had to expand my job search to include potential jobs and industries I would otherwise have never considered," says Tyler Fenelon, a 2010 graduate of UCLA's Anderson School of Management (No. 17). He was able to find the private equity job he'd hoped for. "I consider myself very lucky," he says.

Schools are finding new ways for students to connect with companies that might not recruit on campus. At top-ranked Booth, the employer outreach team has tripled in size, from two to six, in the past two years. Last summer the team met with more than 350 companies, up from 100 in 2007. "We definitely have more corporate relationships now than we did a few years ago," says Julie Morton, associate dean of career services. "We used to assume the relationship began when a company recruited on campus. Now a strong relationship is one where a firm thinks of Booth in terms of sourcing talent—posting a job, coming to campus, or simply interacting with students."

98%

The percentage of students receiving financial aid at Texas A&M's Mays Business School

Schools are also teaming up to bring students to recruiters. In April, 128 students from seven schools—including Michigan's Ross School of Business (No. 7), Cornell's Johnson Graduate School of Management (No. 13), and Notre Dame's Mendoza College of Business (No. 24)—traveled to San Francisco for "A Day in the Bay MBA Interview Forum." The event allowed 36 Bay Area employers, including eBay, Electronic Arts, and the San Francisco Fed, to meet top MBA talent without having to incur the expense of traveling to each campus.

Technology also makes it easier for students to connect with recruiters. At Northwestern University's Kellogg School of Management (No. 4), Skype has become a familiar tool for job seekers, and when Stanford's Graduate School of Business (No. 5) begins its transition into its new Knight Management Center next spring, two Cisco TelePresence videoconference facilities will be available for remote interviews. Videoconferencing

'If the crisis reminded us of anything, it's that free markets and the monetary incentives that underlay them, while incredibly important and powerful mechanisms, can be blunt instruments that don't always inspire prudence, nuance, and care. Twenty-first century leaders must be equipped to navigate unprecedented social and economic complexity and understand that markets alone are not enough.'

—Sally Blount, Dean, Kellogg School of Management, Northwestern University

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For the world's best business schools, 2010 was a year of recovery. In the U.S., Canada, and Europe, jobs and salaries began to bounce back from recession-era lows, and the recruiting landscape shifted subtly. The top 10 U.S. programs were reshuffled and a new international No. 1 was crowned.

Best U.S. Business Schools

2010 Rank	Change from 2008	School	Graduate Poll[1]	Corporation Poll[2]	Intellectual Capital[3]	Tuition & Fees ($)[4]	Pre-MBA Pay ($)[5]	Post-MBA Pay ($)[5]	Selectivity (%)	Job Offers (%)[6]	Career Services[7]	Teaching[7]	Management Skills[8]	Analytical Skills[8]
1	0	**Chicago** (Booth)	2	1	8	103,360	–	102,000	22	91	Excellent	Excellent	Excellent	Excellent
2	0	**Harvard**	5	3	14	112,400	–	110,000	11	95	Excellent	Great	Excellent	Excellent
3	+1	**Pennsylvania** (Wharton)	11	2	13	106,303	75,000	110,000	17	87	Great	Average	Excellent	Excellent
4	−1	**Northwestern** (Kellogg)	6	4	28	102,990	72,000	105,000	19	90	Excellent	Good	Good	Good
5	+1	**Stanford**	7	7	7	106,236	–	120,000	6	93	Great	Good	Good	Great
6	+2	**Duke** (Fuqua)	15	8	1	99,492	59,600	100,000	24	81	Good	Good	Excellent	Excellent
7	−2	**Michigan** (Ross)	16	5	11	100,189	64,000	100,000	25	78	Great	Good	Excellent	Excellent
8	+2	**UC-Berkeley** (Haas)	4	11	5	99,294	72,163	110,000	12	90	Excellent	Good	Great	Great
9	−2	**Columbia**	10	9	12	107,824	–	100,000	15	94	Excellent	Average	Excellent	Excellent
10	−1	**MIT** (Sloan)	3	14	18	101,250	75,000	110,000	13	95	Excellent	Great	Excellent	Great
11	+5	**Virginia** (Darden)	1	16	36	100,000	–	100,000	26	87	Excellent	Excellent	Great	Excellent
12	+6	**Southern Methodist** (Cox)	21	6	40	87,980	50,000	81,000	35	67	Great	Excellent	Excellent	Excellent
13	−2	**Cornell** (Johnson)	8	23	6	98,544	57,500	96,000	23	83	Excellent	Excellent	Great	Great
14	−2	**Dartmouth** (Tuck)	14	15	4	104,700	64,400	105,000	20	97	Great	Good	Great	Great
15	+4	**Carnegie Mellon** (Tepper)	12	20	16	105,000	60,000	95,000	27	89	Excellent	Excellent	Excellent	Great
16	+1	**North Carolina** (Kenan-Flagler)	19	17	26	95,879	51,000	95,000	36	84	Good	Great	Good	Good
17	−3	**UCLA** (Anderson)	17	26	15	97,854	63,000	100,000	29	85	Great	Great	Great	Great
18	−5	**NYU** (Stern)	20	22	19	94,572	65,000	100,000	13	90	Great	Good	Great	Great
19	−4	**Indiana** (Kelley)	26	18	46	90,327	50,875	90,000	42	86	Good	Great	Great	Excellent
20	NEW	**Michigan State** (Broad)	13	32	39	74,580	35,000	86,200	29	72	Excellent	Excellent	Good	Good
21	+3	**Yale**	18	37	9	103,725	60,000	100,000	17	92	Great	Great	Good	Good
22	+1	**Emory** (Goizueta)	22	31	21	84,800	52,013	90,000	33	93	Good	Great	Great	Great
23	+6	**Georgia Tech**	25	30	20	70,716	58,031	85,020	21	97	Excellent	Good	Great	Great
24	−4	**Notre Dame** (Mendoza)	24	33	25	83,997	50,000	90,000	33	82	Great	Excellent	Good	Good
25	−4	**Texas-Austin** (McCombs)	29	29	17	90,856	67,000	95,000	24	93	Good	Good	Great	Great
26	−1	**USC** (Marshall)	9	45	35	97,800	57,000	94,000	22	88	Excellent	Excellent	Good	Good
27	−5	**Brigham Young** (Marriott)	31	19	49	41,120	50,700	88,550	47	87	Good	Great	Good	Good
28	NEW	**Minnesota** (Carlson)	35	21	29	93,449	40,500	90,000	30	91	Great	Good	Good	Good
29	NEW	**Rice** (Jones)	27	44	10	89,620	50,000	95,000	36	84	Great	Great	Good	Good
30	NEW	**Texas A&M** (Mays)	43	13	34	42,925	44,871	85,000	23	92	Average	Great	Excellent	Excellent

Recruiters say Chicago has "the most effective career services office."

Darden is home to the most satisfied students.

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Grads at Stanford make the most money, but it's also the hardest school to get into.

Dartmouth and Georgia Tech grads were the most successful in obtaining job offers.

Best International Business Schools

2010 Rank	Change from 2008	School	Graduate Poll[1]	Corporation Poll[2]	Intellectual Capital[3]	Tuition & Fees ($)[4]	Pre-MBA Pay ($)[5]	Post-MBA Pay ($)[5]	Selectivity (%)	Job Offers (%)[6]	Career Services[7]	Teaching[7]	Management Skills[8]	Analytical Skills[8]
1	+2	**INSEAD**	5	3	2	68,107	–	111,900	–	86	Great	Great	Great	Great
2	−1	**Queen's**	4	5	8	71,000	–	77,944	–	–	Excellent	Excellent	Good	Good
3	−1	**IE Business School**	1	9	14	68,900	62,000	101,000	33	89	Excellent	Excellent	Excellent	Excellent
4	+2	**ESADE**	9	2	16	68,000	52,500	82,000	46	76	Good	Average	Excellent	Great
5	0	**London Business School**	6	7	1	78,842	–	–	18	–	Great	Good	Excellent	Excellent
6	−2	**Western Ontario** (Ivey)	7	6	18	79,120	58,289	84,075	–	92	Great	Great	Great	Good
7	0	**IMD**	2	10	9	82,488	75,000	124,700	22	96	Excellent	Good	Excellent	Excellent
8	0	**Toronto** (Rotman)	16	1	3	99,693	–	80,000	44	–	Average	Good	Great	Good
9	NEW	**York** (Schulich)	13	4	4	58,000	43,400	81,980	26	86	Good	Great	Good	Good
10	NEW	**Cambridge** (Judge)	3	13	12	56,338	–	84,677	27	76	Excellent	Excellent	Average	–

INSEAD claims the top spot for the first time since 2002.

Recruiters love Rotman, but an MBA doesn't come cheap.

Best in category (highlighted)   Excellent   Great   Good   Average

1. RANK BASED ON SURVEYS OF MBA GRADS CONDUCTED IN 2010, 2008, AND 2006, WITH 26,389 TOTAL RESPONSES. CONTRIBUTES 45 PERCENT TO FINAL RANKING. 2. RANK BASED ON SURVEYS OF MBA RECRUITERS CONDUCTED IN 2010, 2008, AND 2006, WITH 680 TOTAL RESPONSES. CONTRIBUTES 45 PERCENT TO FINAL RANKING. 3. RANK BASED ON REVIEW OF FACULTY RESEARCH PUBLISHED OVER 5-YEAR PERIOD IN 20 TOP ACADEMIC JOURNALS AND FACULTY BOOKS REVIEWED IN *THE NEW YORK TIMES, THE WALL STREET JOURNAL*, AND *BLOOMBERG BUSINESSWEEK* OVER SAME PERIOD. CONTRIBUTES 10 PERCENT TO FINAL RANKING. 4. TUITION AND ALL REQUIRED FEES FOR ENTIRE PROGRAM, EXCLUDES LIVING EXPENSES. WHERE APPLICABLE, NONRESIDENT FIGURES USED. 5. SELF-REPORTED BY SCHOOLS. MEDIAN BASE SALARY FOR INCOMING CLASS OF 2010 (PRE-MBA PAY) AND GRADUATING CLASS OF 2010 (POST-MBA PAY) ONLY; DOES NOT INCLUDE SIGNING BONUS, STOCK OPTIONS, OR OTHER COMPENSATION. POST-MBA PAY FIGURE FOR IE BUSINESS SCHOOL IS AN AVERAGE, NOT A MEDIAN. 6. SELF-REPORTED BY SCHOOLS. PERCENTAGE OF JOB-SEEKING 2010 MBA GRADUATES REPORTING AT LEAST ONE JOB OFFER WITHIN 3 MONTHS OF GRADUATION. 7. BASED ON 2010 STUDENT SURVEY. EXCELLENT = TOP 20 PERCENT; GREAT = NEXT 25 PERCENT; GOOD = NEXT 35 PERCENT; AVERAGE = BOTTOM 20 PERCENT. 8. BASED ON 2010 RECRUITER SURVEY. EXCELLENT = TOP 20 PERCENT; GREAT = NEXT 25 PERCENT; GOOD = NEXT 35 PERCENT; AVERAGE = BOTTOM 20 PERCENT. NEW INDICATES A SCHOOL THAT WAS NOT RANKED IN THE TOP 30 U.S. OR TOP 10 INTERNATIONAL IN 2008. IN THAT YEAR, MICHIGAN STATE, MINNESOTA, YORK, AND CAMBRIDGE APPEARED IN AN UNRANKED "SECOND TIER," WHILE RICE AND TEXAS A&M WERE NOT RANKED; THEY LACKED AN ADEQUATE RESPONSE RATE IN ONE OR MORE SURVEYS. DATA: *BLOOMBERG BUSINESSWEEK*, CAMBRIA CONSULTING

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‘Understanding the financial crisis requires appreciating the interconnections between the mortgage market, monetary policy, banking regulations, leadership, corporate governance, and the industrial organization of the financial industry. Students traditionally see different parts of this picture in different courses. We launched an interdisciplinary course, the Future of Financial Services, which challenges them to think about how changes in the present create opportunities for the future.’

—Glenn Hubbard, Dean, Columbia Business School

730
The average GMAT score for incoming MBA students at Harvard Business School

$29K
The average signing bonus of graduates from NYU-Stern, the highest number in the top 30

“gives students an opportunity that they might not otherwise have,” says Cynthia Bush, director of recruiting at Houlihan Lokey, the Los Angeles investment bank. The technology is especially valuable to companies that might hire only a handful of MBAs each year, says Gideon Gradman, vice-president for corporate development at Boston-based Ze-gen, a venture-backed energy startup. “It’s not a perfect replacement for in-person interviews, but it’s an enabling technology for companies like ours that are small and don’t want to be limited geographically.”

Before the job market soured, regional companies would not have been on the radar for many top MBAs, but now career services advisers are recommending that students not limit their job search to a single function, industry, or location. Those who have their hearts set on a “go-to” MBA position in finance should think twice. In late September, Bank of America began laying off employees in its investment banking unit; just a few days later Morgan Stanley announced a hiring freeze in its i-bank group for the rest of 2010. “In the past, students have focused their internship and job search with one specific, singular path,” says Nicole Hall, president of the MBA CSC and executive director of career services at Pepperdine University’s Graziadio School of Business and Management. “Now students have to have a flexible outlook with two or three viable options that they pursue aggressively.”

For some students, the best option is to change course entirely. After watching MBAs from the Class of 2009 at Brigham Young’s Marriott School of Management (No. 27) struggle to find work, Anthony Strike decided to forgo his second year at the school. Instead of accumulating another year of debt, he dove into a full-time job search. After three months he landed a job as product manager at Apria Healthcare in Orange County, Calif. “It was the nontraditional choice,” Strike says, “but it was the right choice for me.”

Students are also being called on to provide assistance to job-seeking classmates. At Chicago, 39 second-year MBAs are serving as career advisers, meeting one-on-one with first-years to share their experiences in the internship and job search. Last spring student leaders at Indiana’s Kelley School of Business (No. 19) created a group informally called the Jobless Lonely Hearts Club. Each week leading up to graduation, about 30 job seekers from the Kelley Class of 2010 met to share leads and commiserate over pizza and beer. Classmates who had already secured employment served as facilitators. “At first it was awkward,” says Darshan Shah, one of the facilitators, “but after those first couple of sessions, we started seeing results. It really brought our class closer together.” Shah says at least five participants ultimately found jobs using contacts picked up from the club.

Happily, there are signs that the job market for MBAs is picking up. More than half of the top programs reported that a higher percentage of students from the Class of 2011 had returned to campus from their summer internships with firm offers. Sectors such as health care and energy are also increasing their full-time job recruiting activity, according to the MBA CSC. Peter Giulioni, assistant dean of career services at the University of Southern California Marshall School of Business (No. 26), expects the recruiting landscape to return to a more traditional model of primarily on-campus recruiting within 18 to 24 months. Good news for the Class of 2012, perhaps, but cold comfort for this year’s graduates. Ⓑ

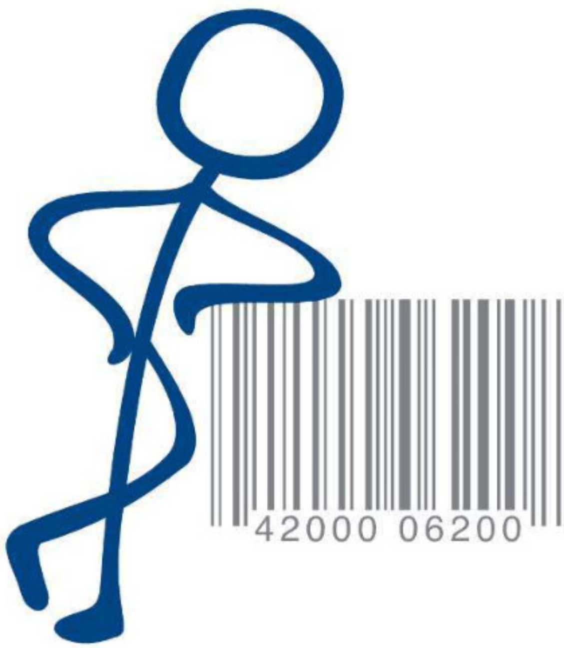
6
Years, 5 Months
Average amount of work experience for students in Yale’s MBA program

‘B-schools are changing how they teach. There are maybe three major lessons. One is managing under uncertainty. Another is public policy: We discovered our students didn’t necessarily know very much about government and public policy. And many schools will have more emphasis on ethics and corporate governance. We’ve been teaching ethics for 30 years, and I think for the ethics and legal studies faculty, this is fodder for their courses.’

—Thomas Robertson, Dean, Wharton School, University of Pennsylvania

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Roger Martin

What We Learned From the Crash

A business school dean describes how his MBA program was shaped and strengthened by the financial crisis, and where it goes from here

If it's true that lessons are learned best when they hit the pocketbook, then my financial education became complete in early 2009, when I received a dry e-mail, with only a faint whiff of apology, from my hedge fund manager. He announced he was shutting down and sending me back the remnants of my investment.

It made perfect sense for him. The standard hedge fund compensation formula is "two and twenty"—2 percent of assets under management and 20 percent of the upside—and he had just lost, along with a hefty chunk of my original investment, his chance at seeing any upside. It wasn't worth his time to strive to get his investors back up to par in exchange for the piddling 2 percent fee.

The lesson for me was that business schools are not doing an awesome job at teaching students about the collision of independent models.

Think about it. My friend's hedge fund was powered by two conflicting sets of business theories. First are financial engineering models that have helped the world understand the power and utility of derivatives. These models, grown initially by finance professors and underpinned by financial and mathematical theory, have helped investors and traders build ever more esoteric instruments for hedging risk—a business' inherent exposure to yen appreciation, for instance—or for making bets on shifts in risks, rates, or returns.

Second is the compensation theory, based on psychology and economics, which holds that two and twenty aligns interests by making sure that if the investors win big, so do the investment managers who made it happen. This theory is conspicuously silent on the lack of alignment when investors lose big—and the only pain for hedge fund managers is the obligation to write short apology e-mails.

I doubt that either the derivatives or compensation theorists appreciated what a potent cocktail they would produce when their theories were sloshed together in the real world. Investment managers use advanced derivatives theory to create instruments with huge and immediate upsides (and of course downsides). In 2007, for example, hedge fund manager John Paulson got Goldman Sachs to create a synthetic portfolio of derivatives, the now-infamous Abacus vehicle, which enabled his fund to make a huge bet against mortgage values. In relatively short order, the investment produced a profit of over $1 billion for Paulson and a commensurate loss for the European banks who bet against him.

Paulson didn't have to worry much about risk. With a flat fee of 2 percent (or more) and $32 billion of assets under management, he would earn $640 million per year even if he lost his clients boatloads of money—hardly the alignment compensation theorists suggested. And the staggering 20 percent upside helped him earn an estimated $3.7 billion in personal compensation in 2007.

For business education, the point is that derivatives theory created the vehicles for taking on massive risk in pursuit of massive compensation, while compensation theory caused managers to have little fear for the downside of that risk. Investment managers chased massive personal gain by incurring huge risks to their investors' capital. By chasing it far enough out the slender tree branch, they crashed the system. Sadly, it was investors, pensioners, and average citizens, not hedge fund managers, who felt the brunt of the fall.

At the Rotman School, lessons of this sort have us redoubling our efforts to help students appreciate how diverse models work together in a broader context. We are teaching them to tear apart the foundations of models, just as an aspiring mechanic would tear down an engine and rebuild it to learn how a car really works. Then they can ask—and answer—questions like: How will the theories I learn in my options and derivatives class intersect with the ones I learn in my organizational behavior class?

We're asking professors and students to tackle complex behaviors head-on, rather than rely on models that assume more simplicity than the real world actually offers. Students need to learn that it is their task to integrate and compare independent systems for themselves, even when academic business theories don't.

We call it Integrative Thinking. We believe it is a habit of mind that will enable students to think their way through the most complex real-world business problems, and even have a fighting chance of averting crises like our current one. On that front, the good news for our first-year students is that in this year's Foundations of Integrative Thinking course, the course of events has furnished them with far more material—real-world examples of clashing and colliding models—than they could have imagined just two years before. Ⓑ

Martin is dean of the Rotman School of Management at the University of Toronto.

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Ryan Austad (quoted & pictured above) is a UNL graduate and currently works with a global consulting firm.

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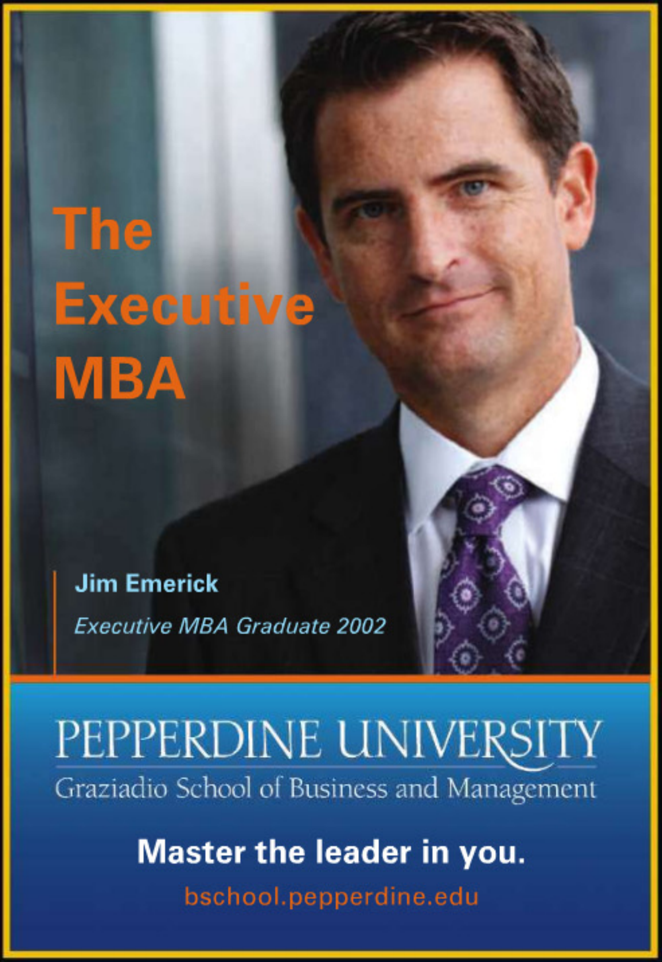
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What does your shirt say about you? Page 92

Shirt Psychology & Wealth & Picasso & Dubya

Etc.



Bush's memoir-cum-management primer Page 100



The Billionaire in the Kitchen

Microsoft's former chief technology officer and his 2,400-page, $625 culinary magnum opus. *By Karl Taro Greenfeld*

BUSH: CAROL T. POWERS/BLOOMBERG VIA GETTY IMAGES; CHEFS: COURTESY OF MODERNIST CUISINE

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Etc. The $625 Cookbook

Of all the eccentric projects a billionaire can embark on—buy a sports franchise and run it into the ground, build a giant wooden aircraft and fly it once, run for high office and alienate half a state—Nathan Myhrvold's is among the more bizarre. For three years the former Microsoft chief technology officer has been on a mission to write, edit, photograph, and publish the world's most comprehensive cookbook. The result: *Modernist Cuisine*, a six-volume, 2,400-page, 48-pound, $625 compendium of contemporary cooking techniques that Myhrvold will publish in March. It is, Myhrvold says, the book he's always wanted to own, if not necessarily bring to the beach. And since he has the means and technological aptitude to create pretty much anything he's ever wanted, it's a good thing he's more interested in cooking than, say, an affordable, suitcase-size thermonuclear device.

In 1999, Myhrvold, a trained physicist who led the development of Windows software and had a net worth of approximately $650 million, took what turned out to be a permanent sabbatical from Microsoft. The next year he left the company altogether and founded Intellectual Ventures (IV), a Bellevue (Wash.)-based incubator of inventions and patents. Myhrvold, 51, subsequently became known for pursuing an eclectic array of scientifically grounded pursuits. Thus far he has embarked on elaborate dinosaur fossil hunts, proposed spraying sulfur particles into the stratosphere to counteract the effects of global warming, and created a surgical stapler able to reach the more inaccessible parts of a patient's body. He's also received more than $5 billion in investment from Apple, Intel, Microsoft, Nokia, and Sony to develop green technologies in developing countries.

Ever wanted to make watermelon look like meat or yucca look like coal?

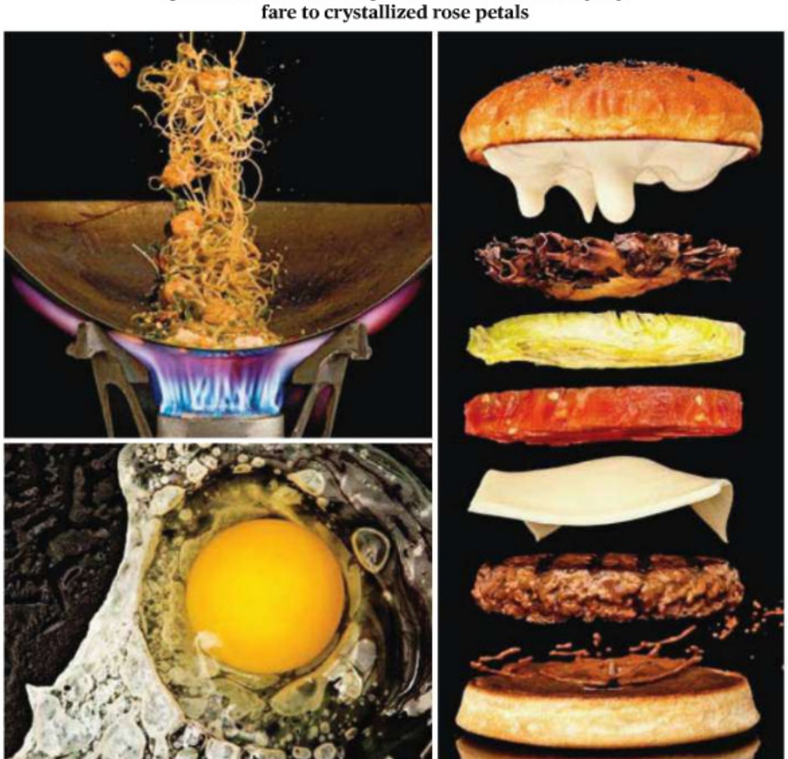
Myhrvold has balanced these pursuits with a lifelong love of cooking. (Another one of IV's quests has been a method for making a better-tasting Pringles-style potato chip.) When he was nine, he single-handedly cooked Thanksgiving dinner for his family from scratch. "I got all these books from the library and taught myself about cooking turkey, stuffing, yams, sweet potato pie," he recalls. In the early 1990s, while still at Microsoft, he attended the renowned Ecole de Cuisine LaVarenne in Burgundy and became an early advocate of modernist chefs such as Ferran Adrià and Heston Blumenthal. Their technique of *sous vide* cooking—the heating of food in sealed, airtight water bags in precisely controlled temperatures—combined Myhrvold's two great passions, science and food, and became a fascination for him. "This style of cooking was raising all sorts of scientific questions, some of which I would sit down and write thousands of lines of code to simulate," he says. "Everyone's intuition was based on conventional wisdom. But these new approaches defied that—and there were no books explaining the science of why you do things or how they work."

So in 2007, Myhrvold created the Cooking Lab, a private company housed within IV, devoted almost entirely to the production—and documentation—of modernist cuisine. He employed dozens of cooks, writers, editors, photographers, and designers and deployed them in what might be the most sophisticated kitchen on the planet. "It won't win any design awards," says Myhrvold, "but in terms of equipment and science, in terms of having to cook anything in the world, yes, it is the best kitchen."

Amid ultrasonic welders, an autoclave designed to sterilize medical equipment, a 100-ton hydraulic press, a rotary evaporator, and hundreds of other gadgets, he and his fellow geeks spent a couple years pushing food science to an extreme only an eccentric billionaire could achieve. "It's not like we were constrained by anything but the calendar," says editor Wayt Gibbs, a former *Scientific American* writer whom Myhrvold lured to the project.

As it turned out, even the calendar didn't prove much of a constraint: The publication date was delayed several times, and the page count grew from 300 to a staggering, and almost farcical, 2,400. Despite the delays, Myhrvold relished the process. After spending his mornings working at IV on, say, an ultracheap pasteurizer for African dairy farmers or a flat-panel antenna using "meta-materials," Myhrvold would spend his afternoons in the Cooking Lab. On any given day, he might saw a pressure cooker in half to take a cutaway photograph or shoot pictures of potatoes that were coated in edible clay to resemble

Comprising six volumes, *Modernist Cuisine* (photos below) has recipes for dishes from everyday fare to crystallized rose petals



worldmags

When Money Doesn't Matter

Think authoring a 2,400-page cookbook is a bizarre hobby? It's only the latest in the ever-diverting line of eccentric mogul hobbies. —*Marnie Hanel*



MICHAEL STEINHARDT

The financier shuttered his $4.4 billion hedge fund–Steinhardt Partners–in 1995 and devoted himself to amassing a private zoo at his Bedford (N.Y.) estate. It includes zebras, camels, and albino wallabies.

SUMNER REDSTONE

The aging Viacom billionaire fell hard for a sexy all-girl band, the Electric Barbarellas, and campaigned–against much resistance–to secure them a reality show last summer on Viacom-owned MTV.





RICHARD BRANSON

Virgin's chairman can't resist a world record. He's sailed the Atlantic and circumnavigated the globe by balloon. He's also crossed the English Channel by amphibious vehicle in 2004 and attempted to kite-board across it for his 60th birthday this year.

WARREN BUFFETT

The Oracle of Omaha has an unlikely affection for soap operas. He's appeared on *All My Children* as "Boo-fay," an adviser to Erica Kane, played by Susan Lucci, on three occasions: in 1991, 1993, and 2008.





PAUL ALLEN

In addition to owning the Seattle Seahawks and collecting military aircraft, the Microsoft co-founder created a $41 million initiative to map the mouse brain. His interest in bug research scored him the namesake, "Paul Allen's Flower Fly."

stones. "The topic changes, but the skill set doesn't," Myhrvold says of his daily transition from inventor to cookbook auteur. "Part of the cookbook has been about reviewing photographs and tasting recipes. Did it taste good enough to go in the book? Obviously, I don't taste things at the flat-panel antenna meeting, so that's different."

Holding the galley pages of his magnum opus, Myhrvold becomes almost giddy as he describes the recipes, the tables, the charts, the history sections, and the photography. (Myhrvold took most of the pictures himself.) He estimates that at one point he had 36 people on his payroll, and while he refuses to put a figure on how much he's spent, he acknowledges it's "millions of dollars." While once describing *Modernist Cuisine* to the staff of a prominent food magazine who didn't quite grasp his pedigree, the editor looked at him quizzically and asked who was subsidizing the project–it must have cost a "million dollars," she said. "I *wish* it only cost a million," Myhrvold replied with a laugh while the room went quiet. As he recalls, "She looked at me, sort of like, 'who the f--- are you?' "

Modernist Cuisine may end up being the most elaborate and complex book ever written–about anything. Like Myhrvold himself, it manages to be exuberant, whimsical, and wildly inventive yet deadly serious. The first five volumes–History and Fundamentals, Techniques and Equipment, Meat and Seafood, Plant Foods, and Plated Dish Recipes–are as complete an exegesis of contemporary cooking as is technologically, financially, and humanly imaginable. The sixth volume–Kitchen Manual–is a 300-page laminated tome designed to withstand a sloppy saucier.

"Maybe the science overwhelmed the gastronomy," Myhrvold concedes

The complete work offers readers a view into Myhrvold's kitchen–and his brain. *Modernist Cuisine* includes recipes for an array of dishes many home cooks may never fathom, such as one that makes watermelon look like meat or another that turns yucca root into something resembling coal. It also provides unique reinterpretations of classics. (Readers can behold a recipe for macaroni and cheese based on wheat beer, sodium nitrate, and iota carrageenan, a gelatin from red seaweed.) There are also recipes for everything in between, from mandarin orange fruit leather to crispy spinach paper and crystallized rose petals. Each page is filled with lavish photographs, punctilious instructions, and a focus on obscure ingredient histories. The images are interspersed with charts and tables befitting an advanced calculus textbook–which was, Myhrvold concedes, sort of inevitable. "Maybe the science overwhelmed the gastronomy," he says with a shrug.

Modernist Cuisine humbly aspires to be to food what Diderot's *Encyclopédia* was to the natural sciences in the 18th century. While some may call it the bible of the kitchen, the cookbook is actually longer than the Bible. (It's also longer than the former bible of the kitchen, *Larousse Gastronomique*, which weighs in at a mere 1,360 pages.) It remains unclear, however, whether there is an audience flush enough to support a six-volume, $625 guide to carbonating a whole piece of fruit. Although *Modernist Cuisine* was born as a passion project, Myhrvold is convinced he can make money from it–eventually. "I would argue this will turn a profit," he says. "I just don't know when." B

OPPOSITE PAGE: IMAGES COURTESY OF MODERNIST CUISINE; THIS PAGE, STEINHARDT: JASON KEMPIN/GETTY IMAGES; CAMEL: BURAZIN/GETTY IMAGES; REDSTONE: BRYAN BEDDER/GETTY IMAGES; TV: RYAN MCVAY/GETTY IMAGES; BRANSON: GUSTAVO CABALLERO/GETTY IMAGES; BALLOON: RICHARD PRICE/GETTY IMAGES; LUCCI: THE KOBAL COLLECTION; BUFFETT: CHINAFOTOPRESS/GETTY IMAGES; TELESCOPE: MICHAEL MATISSE/GETTY IMAGES; ALLEN: LARRY BUSACCA/WIREIMAGE/GETTY IMAGES

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Our Collars, Ourselves

Do you know what your work shirt says about you? *By Darrell Hartman*

As evolving office dress standards have made the suit and tie superfluous in many workplaces, the button-down shirt has become a man's defining fashion statement. "The shirt," says Eric Jennings, men's fashion director at Saks Fifth Avenue, "is where you can express yourself."

With all those men expressing themselves, discerning shirt signals from shirt noise, as it were, has never been more difficult. Particularly because "We're at a moment in the fashion cycle where sport and dress, and business and casual, are colliding," says Jeff Blee, divisional merchandising manager for men's accessories at Brooks Brothers. This means shirts that were once reserved for after work are now becoming commonplace from 9 to 5.

Historically, collars—from the British-inspired spread collar to the casual American button-down—have separated the managers from the managed. These days, though, an array of collar styles, colors, fabrics, weaves, cuffs, and patterns are flooding the workplace. Each shirt communicates something different—but what? *Bloomberg Businessweek* posed that question to a handful of experts, including Blee; Jennings; Sam Spector, a prominent New York City-based stylist; John Minahan, chief executive officer and president of shirtmaker Gitman Bros; and Brett Fahlgren, an established men's style consultant. Next time you get dressed for work, you'll know what statement you're making. Ⓑ

Fig. 1
The Traditionalist

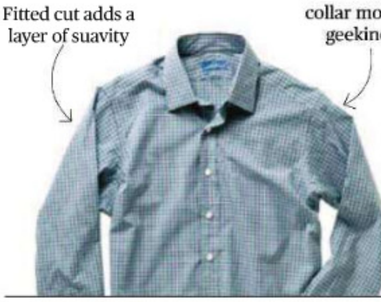




The pinpoint oxford button-down has no prejudices. It's for everyone, from prep-school kids to Warren Buffett. Its wearer is "the sort of guy who doesn't want to stand out in a crowd," says Blee. Leaving collar points unbuttoned, however, makes a "devil-may-care statement," Minahan notes.

Fig. 4
The Dweeb Savant

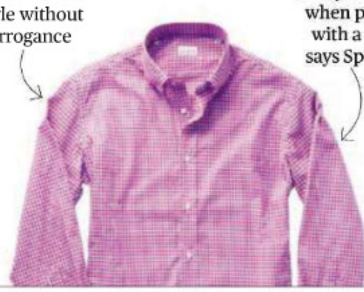




Fitted check shirts are part of the uniform for many of today's upwardly mobile workers. "He's image-conscious and probably in a business where he understands modern media," Minahan says. "He's a tactician—even if his shirt colors aren't always on-trend," Fahlgren notes.

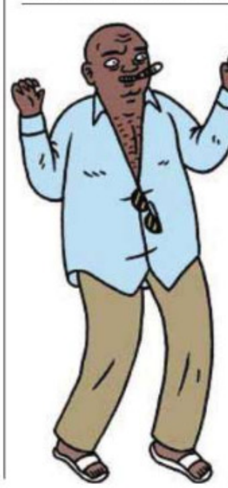
Fig. 7
The Overachiever





A large portion of the American workforce is answering to a thirtysomething in a gingham shirt. "It's really popular right now," Spector says. "The gingham guy is versatile—he's cool, maybe he's a dad," Fahlgren says. "Either way, he's comfortable with who he is."

Fig. 8
The Linen-Loving Playboy





Defying common sense, some men wear linen shirts all year. "It's way too casual for work," Spector says. Worn seasonally with a summer-fabric suit, though, the well-tailored version *can* convey Mediterranean *savoir faire*. However, Minahan says, "Most men don't dare to do it."

PHOTOGRAPHS BY NICK FERRARI FOR BLOOMBERG BUSINESSWEEK; Illustrations by Neil Swaab; 1. Brooks Brothers, $79.50. 2. Ermenegildo Zegna, $325; from Saks Fifth Avenue. 3. Billy Reid, $195. 4. Seize sur Vingt, $200.

Fig. 2

The Loud-Shirt Guy





The associate wearing a party shirt to the morning meeting isn't sending the strongest work vibe. "It's very What-Happens-in-Vegas," says Spector, who recommends pairing this type of shirt with a suit. In the worst-case scenario, Fahlgren notes, "He's wearing it hanging over a bedazzled jeans pocket."

Fig. 3

The Fashionisto





Slim-cut shirts with vintage elements like smaller collars are for younger men who fancy themselves *au courant*, especially when paired with a skinny suit and tie. "He's a natty dresser and probably knows every actor on *Mad Men*," Minahan says. Adds Fahlgren: "He can make you a Southside Fizz."

Fig. 5

The Dressed-By-Wife Guy





Favored by middle-management types on the go, the non-iron shirt is more about ease than style. "I think of the guy in the airport with a computer bag over one shoulder," says Minahan. Adds Fahlgren: "He's practical and professional–there's a good chance his wife buys his clothes for him."

Fig. 6

The Gekko



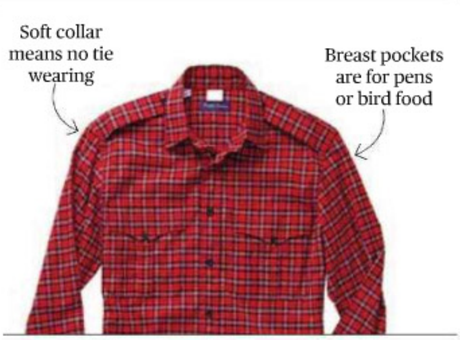


Popularized by Gordon Gekko, the dandyish contrast-collar shirt requires an ego to back it up. "It's a power broker look," Jennings says. Although hip designers have been tweaking this bull-market classic, the usual wearer is still an "older banker or a corporate lawyer," Minahan says.

Fig. 9

The Urban Lumberjack





Not yet entirely welcome in the workplace, the flannel shirt conveys a persona that's part Paul Bunyan and part Polo Ralph Lauren. The shirt signals "a journeyman," says Fahlgren. "Whether or not he rides a mountain bike or goes to the farmer's market, he's looking for something authentic."

Fig. 10

The C-Suite Sartorialist



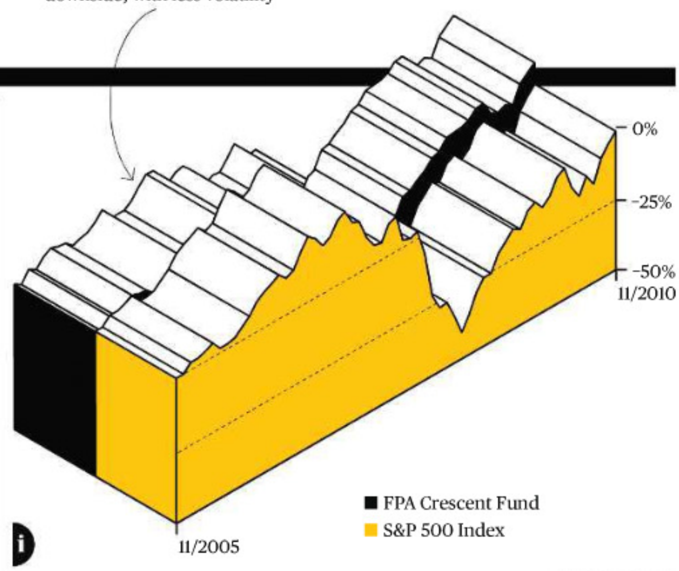


A crisp, expensive, and perhaps monogrammed white or blue dress shirt with modern spread collar is the standard frontispiece of the guy in charge. "He's that much richer and more elegant," Blee says. French cuffs allow more flamboyant honchos to "show off some executive bling," Minahan notes.

5. Brooks Brothers, $79.50. 6. Ralph Lauren Purple Label; $450. 7. Guy Rover; $265; from Barneys New York. 8. Saks Fifth Avenue Men's Collection; $135. 9. Ralph Lauren Purple Label; $450. 10. Thomas Pink; $185.

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Converting Volatility Into Opportunity



FPA Crescent's Steven Romick wants more reward for his fund's risks—and he'll go just about anywhere to find it

Volatility is more a measure of opportunity than risk. It lets me act on the visceral reactions of others. Value is the result of panic selling—irrational, illogical selling. To be good at what we do, we have to be strong financial analysts, strong business analysts, and pretty good psychologists. Our goal, over the long term, is to provide equity-like returns with less risk than the market. We want to make sure the odds and potential payoff are in our favor. If all we can make is 20 percent, but we could also lose 20 percent, then it's not that appealing. If we think we could make 60 percent vs. maybe losing 20 percent, that may be worth the risk. Since the economy is so jacked up on steroids, the fund has a margin of safety. I'm investing in companies we feel can be protected against inflation, with pricing power that could rise as fast as their costs. *—As told to Suzanne Woolley*

THE STATS DATA: BLOOMBERG

Romick launched the $4.1 billion FPA Crescent Fund in 1993. Its 3-, 5-, and 10-year annualized returns (3.1 percent, 6.4 percent, and 12 percent, respectively) are significantly higher than its category average.

Romick on his plays



1. Aon

Aon is the largest insurance broker in the world. They're brokers, not underwriters, so as the price to insure a building goes up, they'll make more money on their commission. The pricing for their products is relatively soft right now. At some point that will change and—given stable pricing and their cost-savings program—we'll make good money. We think interest rates are rising, which would be good for Aon. They have a ton of cash on the books that can be reinvested at a higher rate.



Oiling his joints will cost more

2. Occidental Petroleum

They're a large exploration and production company. It's a business we like because it will benefit from oil being worth more in the future. It's really that simple. Every year you pull oil out, you're depleting your reserve. You then have to buy oil to replace it. Five years ago the oil companies said they'd have X amount in reserves in 2010. Occidental Petroleum is the only large oil company that has actually met their projected reserve replacement—the goals that they laid out for themselves.



3. Mortgage-backed securities

We're buying mortgage loans that originated from 2005 to 2007. The collateral (housing) has fallen out of favor, and some banks don't want to own the loans. We have over 1,000 loans across the country. One was underwritten in Detroit, where we paid $1,800 for the loan and have been paid back $2,500 already. If home prices decline 10 percent, we'd still make at least a 10 percent return—even if these people couldn't stay in their homes. These loans are 3 percent of the fund.



4. CVS Caremark

U.S. health-care spending is likely to grow faster than gross domestic product for the foreseeable future. Big chain pharmacies should continue to take market share from independent drugstores. We like CVS's integrated model—it's a pharmacy and a prescription benefits manager. Prescriptions for generic drugs are increasing at a rate faster than branded drugs, and that's more profitable for pharmacies. CVS's valuation seems reasonable at less than 11 times its expected earnings for 2011.

FROM LEFT: MITCHELL GUNN/NEWSCOM; EVERETT COLLECTION; PETER DAZELEY/GETTY IMAGES; JUPITERIMAGES/GETTY IMAGES

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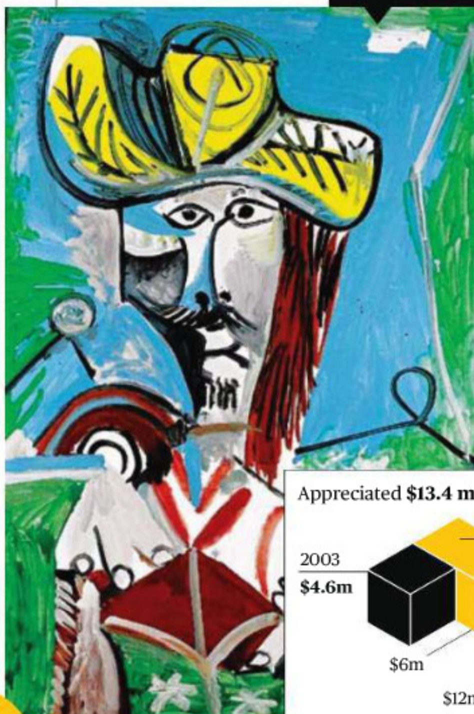
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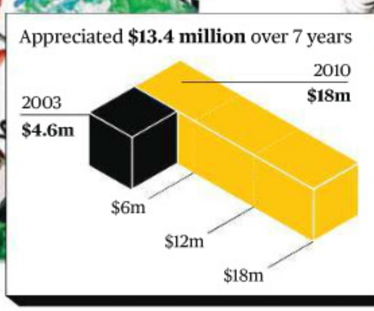
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Etc. Art

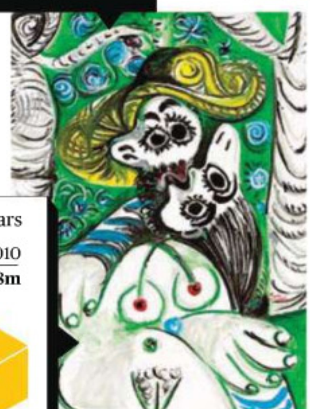
***Buste d'Homme*, 1969**



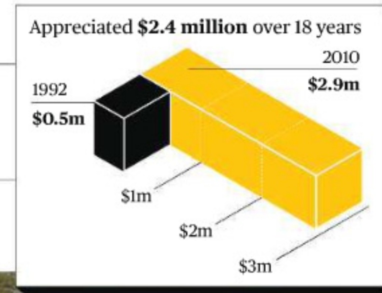
Sold for $10,386,500 at Sotheby's New York on Nov. 4, 2009



***Le Baiser*, 1969**



Sold for $18,011,679 at Christie's London on June 23, 2010



Sold for $2,882,500 at Christie's New York on Nov. 3, 2010



With Late Picasso, Size Matters

Eager Chinese collectors are increasing the demand for Picasso's disparaged later works. *By Rachel Wolff*

Despite Pablo Picasso's reputation as an undisputed genius of modern European art, his brash later works have traditionally received little love from collectors. This may be because the pieces—composed from 1960 until his death in 1973—were long considered, as critic Douglas Cooper once noted, "incoherent doodles done by a frenetic dotard in the anteroom of death." Their unsubtle portrayal of sex suggested to others that they were the aging artist's way of coping in the days before Viagra. For decades, many sold in the low six figures.

In the past two years, though, these large, bright, and loud works have become sensations. In a perfect marriage of questionable taste and label snobbery, newly wealthy Chinese collectors are flocking to late Picassos and helping drive prices to unprecedented levels. What's the allure? Well, they're large, bright, and loud—and, of course, they were painted by Picasso. "There is something about these works that definitely appeals to the Chinese," says Ken Yeh, Christie's Asia chairman. "Many of the late Picassos are very colorful and big in scale. In Asia, they generally prefer larger paintings. Size does matter."

Eager to capitalize on the desires of Chinese collectors who are moving into just about every category of the art market these days, major dealers and galleries are papering their walls with late Picassos. Many of the works are coming from American and European collectors who acquired them in the 1970s, '80s, and '90s, and appear eager to cash in on the boom. Artist and filmmaker Julian Schnabel, for example, unloaded a massive 1971 work for $7.7 million at Christie's New York last year. In March 2009, megadealer Larry Gagosian mounted a museum-caliber exhibition of late Picassos in one of his New York galleries. Two months later, Christie's New York sold Picasso's bright, misshapen *Mousquetaire à la Pipe* (1968) for $14,642,500—more than twice what it sold for in 2004. In June, Sotheby's London sold Picasso's *Homme à l'Epée* (1969) for $7 million; that same month, Christie's London sold his *Le Baiser* (1969) for a little over $18 million—$13 million more than paper mogul Peter Brant paid for it in 2003.

Last week, Christie's and Sotheby's

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***Le Peintre et Son Modèle*, 1964**



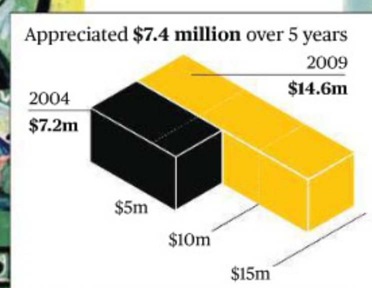
***Tete de Femme (Jacqueline)*, 1963**

Sold for $12,887,348 at Christie's London on Feb. 2, 2010



***Mousquetaire à la Pipe*, 1968**

Sold for $14,642,500 at Christie's New York on May 6, 2009





***Femme au Grand Chapeau*, 1965**

Sold for $9,322,500 at Sotheby's New York on May 5, 2010

DATA: CHRISTIE'S, SOTHEBY'S

achieved similar results at their New York auction houses with Chinese collectors bidding aggressively on most lots. Christie's sold Picasso's *Faune, Femme Nu et Mousquetaire*, a raunchy drawing made in 1967, for $1.3 million—$500,000 more than its presale estimate—as well as the 1964 painting *Le Peintre et Son Modèle*, which met heightened expectations by fetching nearly $3 million. At Sotheby's, Picasso's *Homme au Fanion* (1969) brought in $5.4 million. "It's a very sound market and a very real market," says Giovanna Bertazzoni, the head of Modern and Impressionist art at Christie's London. "It's not a bubble."

The works do offer distinct charms for newly ascendant collectors. They're less expensive than trophy pieces from the artist's Blue Period, which typically sell for upwards of $20 million. Melissa Chiu, director of the New York-based Asia Society Museum, also believes they befit certain lifestyle preferences. "It's a broader socioeconomic trend," Chiu says. "The Chinese collectors at this level have a great interest in European culture. They want to acquire those kinds of cultural values. You need only look at the high-end housing complexes in China—they're in a European style. They even have European names." Chiu notes that these collectors are moving into other European-dominated areas of connoisseurship as well, fine wines among them.

There's also a larger aesthetic reappraisal playing out in the background. In the past few years, some scholars have begun viewing the violent brushstrokes and disorderly compositions that characterize Picasso's later works as akin to popular midcentury trends such as abstract expressionism, Pop art, and even graffiti. Christie's Bertazzoni notes the similarities between late Picassos and increasingly popular contemporary Chinese paintings, particularly in the use of caricature and a subliminally disenchanted political tone.

Although it's too soon to tell whether these aesthetic connections will remain valid, experts note that it hardly matters when pieces are selling for 500 percent more than what they fetched a decade ago. "I was in Hong Kong and Beijing in the weeks leading up to last week's sales," says David Norman, the executive vice-president of Impressionist and Modern art at Sotheby's. "All I heard was, 'What Picassos are being sold?' "

With this season's crop of Modern and Impressionist sales behind them, Christie's and Sotheby's are both in consignment mode, securing work for their major February sales in London. And given the proclivities of their new collectors, they'll keep at least three important attributes in mind: The Picassos will be large, colorful, and expensive. B

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Etc. One True Thing

The Transition Bag

A convertible satchel that morphs from workday to out-at-night. *By Doria Santlofer*

The Want: An all-purpose bag that's roomy enough for office must-haves yet sophisticated enough to carry to after-work cocktails or a client dinner. It's got to be versatile, and had better be chic, too.

The Get: Rachel Nasvik's Phoebe bag ($335 at rachelnasvik.com). By day, the purse can hold everything from lunch Tupperware to commuting flats. For a dressier evening look, the shoulder strap detaches to transform it into a ladylike shape. With two zippered outside pockets, there are no excuses for rummaging around to find your office ID badge. Best of all, Nasvik's buttery leather improves with age. B



BAG LADY ESSENTIALS

These purse accessories will take you from the cube to the club



Touch Up

Make up and go with Trish McEvoy's new Mobile Beauty Emergency kit. It contains blush, lip gloss, and two mini lucite-handled brushes–all housed in a sleek black quilted case that's big enough to hold a smartphone. *$68 at trishmcevoy.com.*



Roll Up

Ditch your high heels at the end of the night and step into FootzyRolls flats. These compact shoes fold into a zip-up pouch that's small enough to fit into a clutch. They also come with a a drawstring bag for storing your stilettos. *$19.99-$30 at footzyrolls.com.*



Open Up

Weather the storm with a lightweight and sturdy Jacobs by Marc Jacobs patterned umbrella. Best of all, once the rain clears up, it's tiny enough to be slipped inside its carrying case and stashed in your purse. *$18 at Marc by Marc Jacobs, 212 924-6126.*

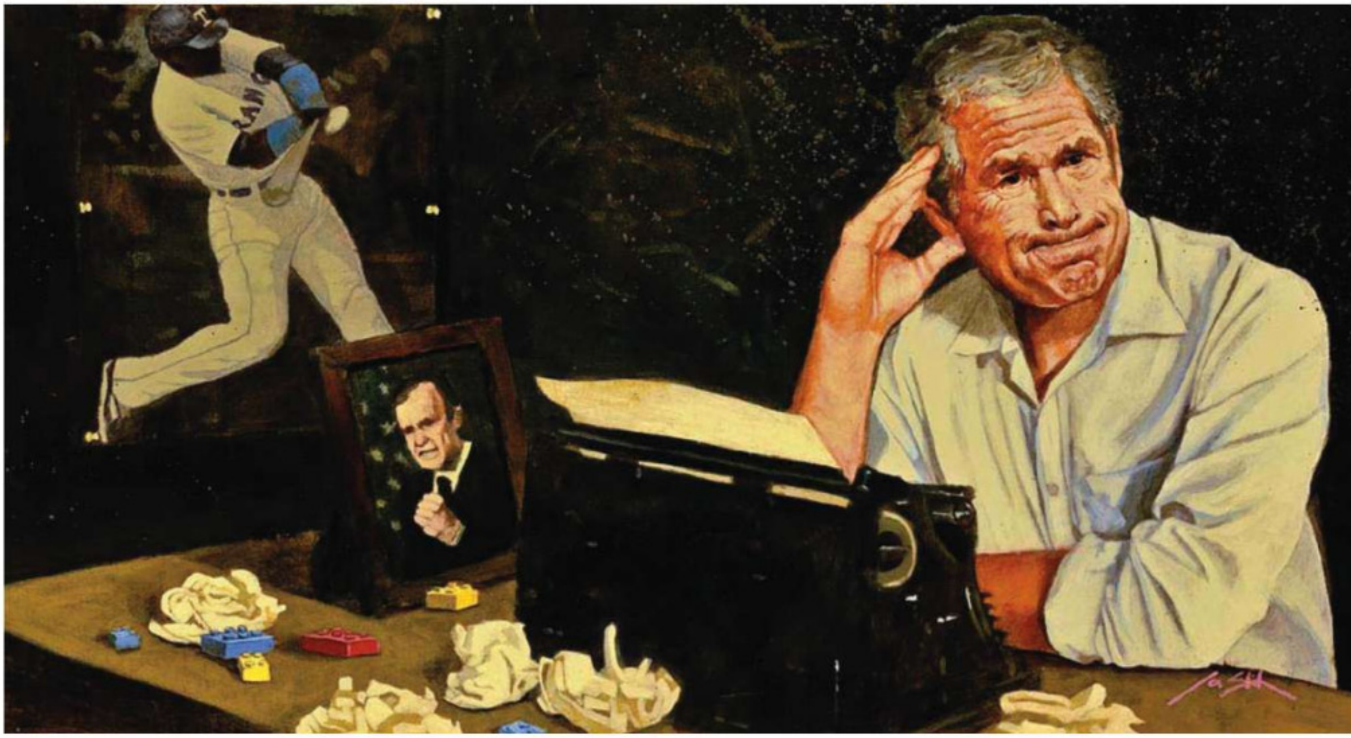


Zip Up

Store your evening baubles in these Rebecca Minkoff leather pouches, complete with custom hardware, a soft lining, and whimsical French phrases. They're perfect for odds and ends such as change, debit cards, and lipstick. *$55 at rebeccaminkoff.com.*

BAG: PHOTOGRAPH BY PLAMEN PETKOV FOR BLOOMBERG BUSINESSWEEK

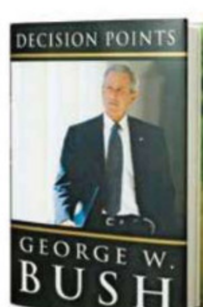
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The Either-Or Presidency

In his memoir and management primer, Bush makes decisiveness the only virtue. *By Drake Bennett*

Decision Points
By George W. Bush
CROWN
512pp, $35



Midway through his second term as President, George W. Bush again found himself under pressure to fire Donald Rumsfeld, his embattled Defense Secretary. In a Rose Garden press conference, Bush praised Rumsfeld's performance and succinctly explained his rationale for keeping him on the job. Bush had heard the criticism, he insisted, but he knew what was right: "I'm the decider, and I decide what is best."

Seven months later, Rumsfeld was gone. As we learn in Bush's new memoir, being decisive is sometimes less important than just looking decisive.

During his eight years in office, the Decider chose to invade two countries, expand Medicare, reshape the American education system, and temporarily take over the national banking system and automobile industry. After leaving the White House, he decided to set his memoir apart by not writing a mere blow-by-blow account for future historians. As befits the nation's first MBA president, *Decision Points* is, for better or worse, a management book. Bush breaks his Presidency up into a series of decision-making case studies; some chapters have titles like "Afghanistan" and "Stem Cells," while others are labeled "Leading" and "Personnel." The result is a book that owes as much to Jack Welch's *Straight from the Gut* as it does to Harry Truman's memoirs—with a bit of Dr. Phil thrown in. "I hope this will give you a better sense of why I made the decisions I did," Bush writes. "Perhaps it will even prove useful as you make choices in your own life."

Many readers will be familiar with the decision-making stratagems in the book because they're the same ones Bush cited while in office. He devotes 50 pages to his decision to invade and occupy Iraq without proof that Saddam Hussein possessed weapons of mass destruction, yet sheds no new light on the matter. Now, as then, he argues that Social Security was unfairly burdening our children with debt, that the Surge would give Iraq the stability to form a functioning society, and that John Roberts is a brilliant lawyer of impeccable character. Sprinkled among these are commonsense observations about leadership: "Timeliness is important to make sure an organization does not get sloppy,"

Bush writes—proof that his trademark diction survived the editing process. Also: "The first step of any successful crisis response is to project calm."

More interesting are the passages where Bush reviews decisions he regrets. In many of these he remains convinced he was right on the merits but simply failed to take into account the potential spin: his failure to visit Louisiana in the first days after Katrina, his theatrical "Mission Accomplished" speech, his "Bring 'em on" provocation to Iraqi insurgents, and the Harriet Miers nomination. As he writes, "While I know Harriet would have made a fine justice, I didn't think enough about how the selection would be perceived by others."

As with the Miers debacle, Bush suggests that faith in his own instincts has sometimes blinded him to the crosscurrents of popular perception. He's less aware of how other decisions, in his own recounting, are shaped by an acute sensitivity to public opinion. One of *Decision Points*' key revelations is that Bush considered replacing Rumsfeld as early as 2004. Nonetheless, he left him in charge of the faltering effort to stem the Iraqi insurgency for two more years.

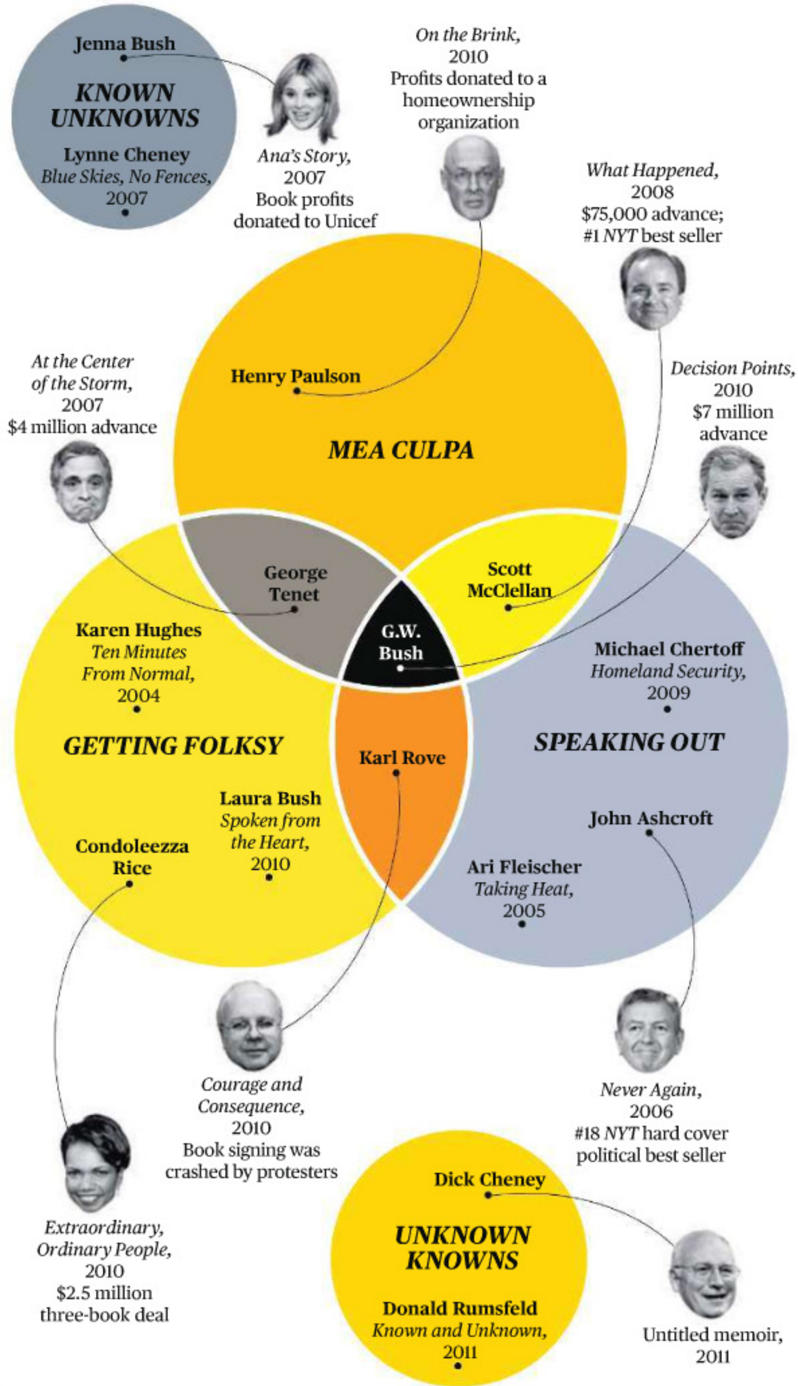
This wasn't just a gut call. Bush says he resisted making the change sooner in part because it would have looked like a capitulation to the retired generals calling for Rumsfeld's ouster. "There was no way I was going to let a group of retired officers bully me into pushing out the civilian secretary of defense," he writes. "It would have looked like a military coup and would have set a disastrous precedent." Instead, he stuck with the status quo until after the 2006 midterm elections, then accepted Rumsfeld's resignation.

As a handbook for aspiring leaders, *Decision Points*' main shortcoming is embedded in its premise. Making tough calls is an important part of what a leader does; it's not the only thing. As both an author and President, Bush sees decisions as discrete "points" to be attacked and only revisited between hardcovers. Unfortunately, running a country, like running a business, isn't just a series of decisions, and viewing it that way obstructs a leader's other responsibilities. The major failures of the Bush Administration—whether it was the bloody chaos of the early occupation of Iraq, the inability to establish a just system to detain and try suspected terrorists, or the collapse of Social Security reform—resulted from poor decisions. Yet they also sprung from failures to address other requirements of good management: planning for contingencies, resolving conflicts between subordinates, and making sure that decisions, once made, were properly implemented and revisited after the fact.

It remains to be seen whether Bush's successor, with his more deliberative style, can handle his own challenges any better. If the Bush Administration has shown us anything, though, it's the perils of seeing decisiveness as its own reward. **B**

The Bush Book Industry

In addition to launching two wars, George W. Bush has also given rise to a veritable literary genre. Herewith, a breakdown of the authors who have emerged from his inner circle to make a buck, make a fuss, or repent.



OPPOSITE PAGE: ILLUSTRATION BY JON STICH; THIS PAGE CLOCKWISE FROM TOP: ANDREW HARRER/BLOOMBERG; TIM SLOAN/AFP/GETTY IMAGES; ROGER L. WOLLENBERG-POOL/GETTY IMAGES; BRENDAN HOFFMAN/GETTY IMAGES; MATTHEW CAVANAUGH/GETTY IMAGES; TAYLOR HILL/FILMMAGIC/GETTY IMAGES; KEVORK DJANSEZIAN/GETTY IMAGES FOR ESPY; ALEX WONG/GETTY IMAGES FOR MEET THE PRESS; CHRIS GORDON/GETTY IMAGES

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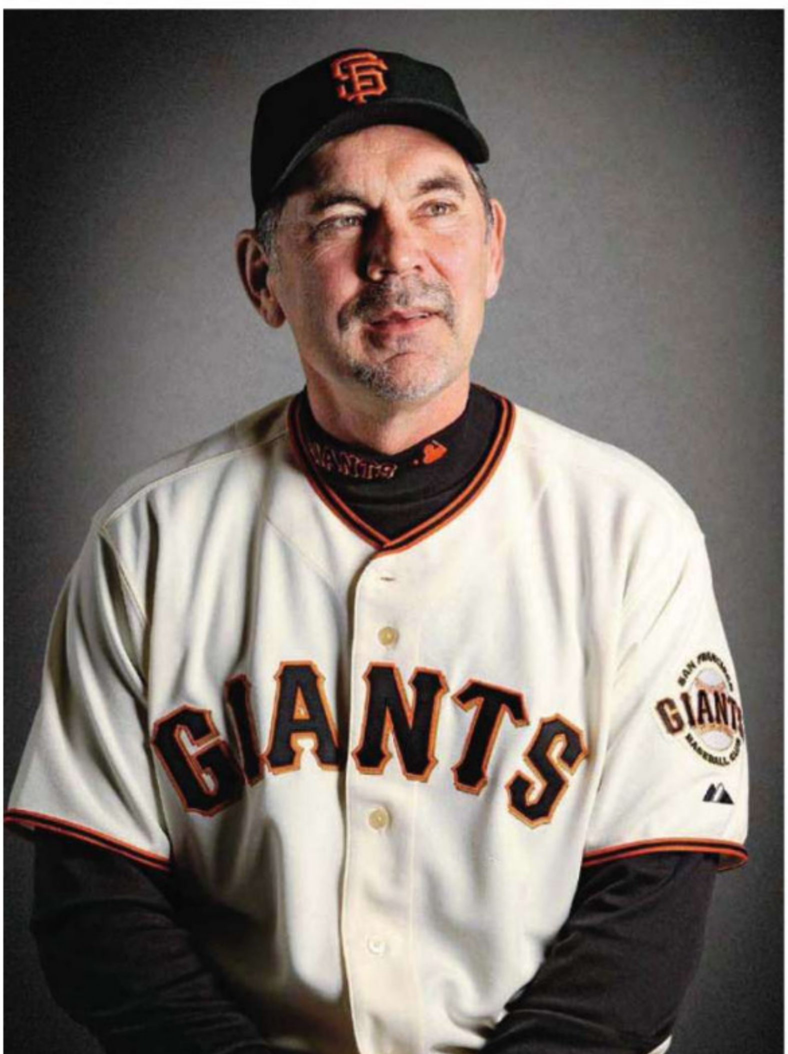
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Etc. Hard Choices

Bruce Bochy

“Telling a starter that he’s now going to be on the bench isn’t easy. You’re not just dealing with egos; you’re dealing with good players”

The San Francisco Giants manager on tweaking his lineup, benching veterans, and leading his team to a championship



Coming into this season, we were optimistic. We felt we had a team that could contend and a pitching staff that could take us to the post-season.

Like any job, the more you learn, the better manager you become. I was like any young manager when I started out. I was a lot harder on players than I am now. I’ve learned to be patient: The longer you do this, the more you understand you’re going to have critics and second-guessing.

When you’re in the World Series, your decisions are going to be looked at closely. The toughest part of a manager’s job is when you have to change the role a player’s accustomed to having. Telling a starter that he’s now going to be on the bench isn’t easy. You’re not just dealing with egos; you’re dealing with good players who are used to going out there every day.

The most difficult decision I made came when I was setting up the playoff pitching roster. Barry Zito is a good pitcher who was instrumental in getting us to the postseason, but I had to leave him off. We went with a four-man rotation, and I felt we had to go with the four pitchers who were throwing the ball the best. I was honest and straightforward with Zito. He understood that he wasn’t throwing the ball as well. He held himself accountable, and I admire him for that.

I made some other changes, but I had the personnel who could accept them. Players might not have been happy about it, but they bought into it and did what was best for the team. Aaron Rowand had been our starting center fielder, but Andres Torres got a chance to play every day, and he shined. That relegated Aaron into more of a part-time role. Torres became our lead-off hitter, and that helped change our club.

The beauty of this game is that so many people have played it, watched it, and loved it. Second-guessing comes with the territory, and I’d much rather have second-guessing than apathy. Right now, people are saying that I made good decisions, but it always comes down to the players. My job is to put them in a position where they can succeed. They make the decisions look right. B *—As told to Diane Brady*

JED JACOBSOHN/GETTY IMAGES



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